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Overstretched, overwhelmed and over there

The sorry state of Britain's armed forces



Print edition January 31st 2009

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The slump in East Asia was made at home as well as in the West: leader



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Politics this week

Jan 29th 2009
From The Economist print edition

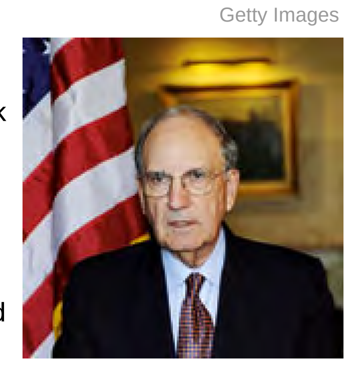
America's House of Representatives voted by 244 to 188 in favour of Barack Obama's $819 billion economic **stimulus package.** Not a single Republican supported the plan (11 Democrats also voted against it). The Senate will now work on the measure. Mr Obama earlier began detailing how some of the money would be spent, such as adding 3,000 miles of electric transmission lines and doubling America's use of wind and solar energy. See article

Mr Obama had a frenetic first week as president, signing a measure that restores funding for health groups that perform **abortions** in developing countries (a ban that had been popular with conservatives) and issuing orders to toughen **fuel-efficiency** standards. See article

The Senate voted to confirm **Tim Geithner** as treasury secretary by 60-34. Most Republican senators withheld their support because of Mr Geithner's "careless" past failure to pay Social Security and Medicare taxes.

Good luck

Getty Images



Foreign leaders and diplomats, including Barack Obama's newly appointed envoy to the Middle East, George Mitchell, gathered in Egypt in an effort to consolidate a fragile ceasefire after Israel's three-week war in Gaza, and to seek ways of fixing a more durable peace between **Israel** and **Palestine**. See article

Iran's president, Mahmoud Ahmadinejad, responded to an overture by Mr Obama on an Arabic television channel by angrily calling for an apology for past American "crimes" against Iran. Mr Obama, who offered during his inauguration to extend the hand of friendship if Iran (and others) "unclench [their] fists", had aired the possibility of softening America's policy to Iran.

Zimbabwe's president, Robert Mugabe, and the leader of the opposition, Morgan Tsvangirai, agreed to implement a power-sharing deal, whereby the latter would become prime minister and the former would remain president. Mr Tsvangirai's party may yet reject the deal, as it lets Mr Mugabe control the key ministries. See article

After months of delay, the first trial at the **International Criminal Court** in The Hague began. A former Congolese warlord, Thomas Lubanga, pleaded not guilty to charges that he recruited and used child soldiers to kill, pillage and rape. See article

In harm's way

Concerns mounted about the fate of an estimated 250,000 civilians trapped in fierce fighting between the **Sri Lankan army** and the rebel Liberation Tigers of Tamil Eelam in the north of the country. The army announced the capture of Mullaitivu, the Tigers' last big stronghold. See article

Parliament in **Bangladesh** reconvened for the first time since an election in December ended two years of rule by an army-backed interim government. The session was marred when the opposition walked out. The ruling Awami League easily won subdistrict elections, which were tarnished by violence and vote-rigging. See article

India's prime minister, **Manmohan Singh**, was said to be making a speedy recovery after undergoing heart-bypass surgery. His Congress party said he would still lead it into a general election due by May.

Kim Jong Il, **North Korea's** dictator, met a foreign visitor—a senior Chinese official—for the first time

since being reported abroad to have suffered a stroke in August. Speaking in Macau, Mr Kim's eldest son said his father was healthy.

After months of debate, **Japan** became the latest country to announce the deployment of its navy to protect commercial ships from pirates off Somalia. The sort of force that will be needed is still being assessed.

Afghanistan's election commission announced that the presidential election, due in May, will not be held until August. A lack of security has prevented voters from registering in parts of the country.

Depressed in Davos

Politicians, businessmen and the press met sombrely in Davos for the annual **World Economic Forum**, reflecting the global economic crisis. The Russian and Chinese prime ministers, Vladimir Putin and Wen Jiabao, attacked the West for causing the trouble.

Reuters



Iceland's government became the first to fall as a result of the financial crash. After continued street protests over the government's handling of the banking crisis, the prime minister, Geir Haarde, resigned. His coalition partner, the Social Democrat alliance, is forming a new government, though an early election is still expected in May. See article

Farmers in **Greece** stepped up their blockade of main roads, obstructing trade and traffic both in Greece and from its neighbours. The farmers want more government subsidies.

Russia hinted that it would abandon its plans to station short-range missiles in Kaliningrad. The move reflects a hope in the Kremlin that the Obama administration may delay the deployment of missile defences in Poland and the Czech Republic. See article

Russian bishops chose Metropolitan Kirill of Smolensk, an assertive figure in religious diplomacy, to be the new patriarch of the **Russian Orthodox** church.

Morales persuasion

In a victory for Evo Morales, **Bolivia's** socialist president, 62% of voters backed a new constitution that he hopes will give greater rights to Amerindians, tighten state control over the economy and limit landholdings to 5,000 hectares (12,400 acres). But a majority of voters in four resource-rich eastern departments that have declared their autonomy rejected the constitution, which may presage future conflicts.

Canada's Conservative minority government announced an expansionary federal budget involving the first fiscal deficit since 1996, together with a bigger buy-up of mortgage-backed securities, in an effort to offset the economic slowdown. Opposition parties criticised some of the details of the budget, but seemed unlikely to try to bring the government down. See article

Mexico's army said it had arrested a man who confessed to dissolving the bodies of 300 people in acid over the past decade while working for a drug-trafficker in Tijuana.

AP

Around 100,000 anti-globalisation activists gathered in the Brazilian city of Belém for the **World Social Forum**. The event takes place each year as an alternative to the more business-friendly affair in Davos.



Business this week

Jan 29th 2009
From The Economist print edition

Pfizer agreed to pay $68 billion for **Wyeth**. The acquisition, one of the biggest ever in the drugs industry, raised expectations of more consolidation. Around a third of the deal will be funded by debt, the remainder by stock and cash reserves. Coming amid the worst financial crisis in decades, the announcement provided stockmarkets with some welcome relief from the steady beat of glum news. See article

Pfizer was, however, among a number of companies that announced huge **job cuts**. The total ran to tens of thousands, including 65,000 in America in a single day. The International Labour Organisation, a UN agency, forecast that the number of unemployed people in the world would be higher by 18m this year than in 2007, but if its "worst-case scenario" came to pass the figure could be 50m. See article

Announced job cuts
Selected companies, January 2009

Company	Job cuts
Caterpillar	20,000
Home Depot	7,000
ING	7,000
Microsoft	5,000
Pfizer	8,300
Philips Electronics	6,000
Sprint Nextel	8,000
Starbucks	6,700

Source: Press reports

The IMF's chief economist said 2009 would be the world economy's worst year since 1945. The fund reduced its forecast of **global GDP** growth to 0.5%, from the 2.2% it predicted last November. The United States' economy is expected to shrink by 1.6%, the euro area's by 2% and Japan's by 2.6%. The IMF predicts that Britain's economy will be the worst performer among big industrial nations, contracting by 2.8%. See article

Boeing confirmed it was shedding 10,000 workers when it reported a $56m net loss for the fourth quarter. A long strike by machinists hurt production, which could suffer further if airlines cancel or defer orders during the downturn. Boeing recorded 662 net commercial-aircraft orders in 2008 (behind Airbus's 777 net orders), down sharply on the 1,413 it scored in 2007.

Simply staggering

John Thain's departure from Bank of America continued to reverberate. Mr Thain stepped down as head of the bank's global banking and wealth management division after it emerged that Merrill Lynch, which he once led, made a $15 billion loss in the fourth quarter, causing BofA to ask for more state aid to fund its acquisition of the Wall Street firm. It also surfaced that Merrill accelerated some $4 billion in bonuses to staff before the completion of the government-backed takeover.

Meanwhile, Mr Thain admitted that spending $1.2m on **refurbishing his office** last year was "a mistake in the light of the world we live in today". A $1,400 waste-paper basket was on the list of new items. See article

New York state's comptroller said that **bonuses** paid by Wall Street firms to their New York City employees (residents and commuters) fell by 44% in 2008, costing the state $1 billion in lost tax revenues and the city $275m.

Nomura's quarterly loss of ¥343 billion ($3.7 billion) was its biggest since it adopted American accounting standards in 2001. The Japanese brokerage was hit by a triple blow: absorbing Lehman Brothers' European and Asian business, which it bought after the investment bank's demise; exposure to the collapse of Icelandic banks; and costs associated with Bernard Madoff's alleged Ponzi scheme.

Proactive action

Santander offered to recompense private-banking clients who lost money in one of its funds that invested with Mr Madoff and said it would fork out €1.4 billion ($1.8 billion) in compensation. Observers were unsure if this would stop investors from suing the Spanish bank; a class-action lawsuit had just been lodged in a Florida court. Santander is the first financial company to offer to settle claims resulting from

the Madoff scandal.

ING's chief executive resigned when the Dutch bank said it expected a big quarterly loss and would seek further government assistance.

ConocoPhillips reported a $31.8 billion net loss for the fourth quarter, mostly related to charges it took on writing down exploration and production assets it bought in 2006 and on its investment in Russia's Lukoil (Conoco's adjusted earnings were $1.9 billion).

Sony's profit plummeted in the last three months of 2009. The Japanese electronics giant is on course to make a record annual loss.

Some £2.3 billion ($3.2 billion) was extended in loan guarantees to Britain's **car industry**. The government stressed it was not a bail-out. Unions and business leaders said it was not enough, considering the vast sums of public assistance given to the country's banks. See article

About to be pecked to death?

Investors responded positively to **Yahoo!'s** quarterly earnings. The internet company made a net loss of $303m; without charges and write-downs, it turned a profit of $238m. Carol Bartz, the new chief executive, said she was contemplating the future of Yahoo!'s search business, which Microsoft is interested in buying, but reflected that "this is not a company that needs to be pulled apart and left for the chickens."

KAL's cartoon

Jan 29th 2009
From The Economist print edition

Illustration by KAL



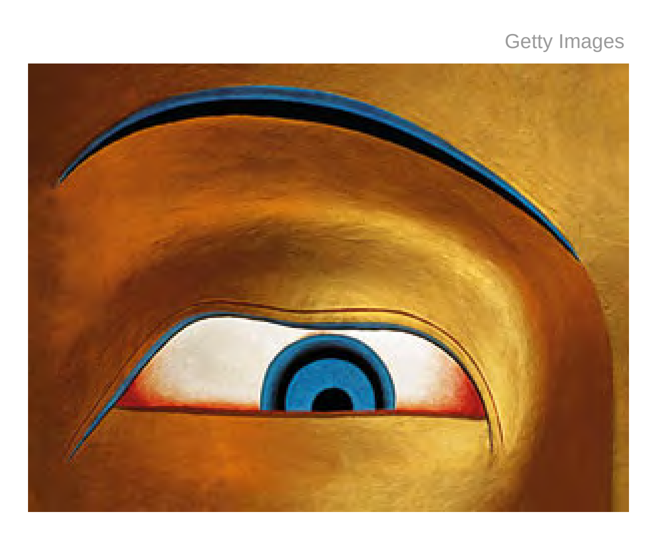
Asia's sinking economies

Asia's suffering

Jan 29th 2009
From The Economist print edition

The slump in East Asia was made at home as well as in the West

Getty Images



CHINA's lunar new year sees the world's largest migration, as tens of millions of workers flock home. Deserting for a few days the factories that make the goods that fill the world's shops, they surge back to their native villages. This week, however, as they feasted to the deafening rattle of the firecrackers lit to greet the Year of the Ox, their celebrations had an anxious tinge (see article). Many will not have jobs to go back to.

China's breakneck growth has stalled. The rest of East Asia, too, which had hoped that it was somehow "decoupled" from the economic trauma of the West, has found itself hit as hard as anywhere in the world—and in some cases harder. The temptation is to see this as a plague visited on the region from outside, which its governments are powerless to resist or cure. In truth, their policy errors have played their part in the downturn, so the remedies are partly in their hands.

The scale and speed of that downturn is breathtaking (see article), and broader in scope than in the financial crisis of 1997-98. China's GDP, which expanded by 13% in 2007, scarcely grew at all in the last quarter of 2008 on a seasonally adjusted basis. In the same quarter Japan's GDP is estimated to have fallen at an annualised rate of 10%, Singapore's at 17% and South Korea's at 21%. Industrial-production numbers have fallen even more dramatically, plummeting in Taiwan, for example, by 32% in the year to December.

Nobody's buying it

The immediate causes are plain enough: destocking on a huge scale and a collapse in exports. Even in China, exports are spluttering, down by 2.8% in December compared with the previous year. That month Japan's fell by 35% and Singapore's by 20%. Falls in imports are often even starker: China's were down by 21% in December; Vietnam's by 45% in January. Some had suggested that soaring intra-regional trade would protect Asia against a downturn in the West. But that's not happening, because trade within Asia is part of a globalised supply chain which is ultimately linked to demand in the rich world.

Some Asians are blaming the West. The Western consensus in favour of globalisation lured them, they say, into opening their economies and pursuing export-led growth to satisfy the bottomless pit of Western consumer demand. They have been betrayed. Western financial incompetence has trashed the value of their investments and consumer demand has dried up. This explanation, which absolves Asian governments of responsibility for economic suffering, has an obvious appeal across the region.

Awkwardly, however, it tells only one part of the story. Most of the slowdown in regional economic growth so far stems not from a fall in net exports but from weaker domestic demand. Even in China, the region's top exporter, imports are falling faster than exports.

Domestic demand has been weak not just because of the gloomy global outlook, but also because of government policies. After the crisis a decade ago, many countries fixed their broken financial systems, but left their economies skewed towards exports. Savings remained high and domestic consumption was suppressed. Partly out of fright at the balance-of-payments pressures faced then, countries have run large trade surpluses and built up huge foreign-exchange reserves. Thus the savings of poor Asian farmers have financed the habits of spendthrift Westerners.

That's not all bad. One consequence is that Asian governments have plenty of scope for boosting domestic demand and thus spurring economic recovery. China, in particular, has the wherewithal to make good on its promises of massive economic stimulus. A big public-works programme is the way to go, because it needs the investment anyway. When Japan spent heavily on infrastructure to boost its economy in the early 1990s, much of the money was wasted, because it was not short of the stuff. China, by contrast, could still do with more and better bridges, roads and railways.

Safety in numbers

Yet infrastructure spending alone is not a long-term solution. This sort of stimulus will sooner or later become unaffordable, and growth based on it will run out of steam. To get onto a sustainable long-term growth path—and to help pull the rest of the world out of recession—Asia's economies need to become less dependent on exports in other ways.

Asian governments must introduce structural reforms that encourage people to spend and reduce the need for them to save. In China, farmers must be given reliable title to their land so that they can borrow money against it or sell it. In many countries, including China, governments need to establish safety-nets that ease worries about the cost of children's education and of health care. And across Asia, economies need to shift away from increasingly capital-intensive manufacturing towards labour-intensive services, so that a bigger share of national income goes to households.

For Asian governments trying to fix their countries' problems, the temptation is to reach for familiar tools—mercantilist currency policies to boost exports. But the region's leaders seem to realise that a round of competitive devaluation will help no one. China has responded to American accusations of currency "manipulation" by denying it has any intention of devaluing the yuan to boost exports. Structural reforms to boost demand would not only help cushion the blow to Asia's poor and thus help avert an explosion of social unrest that governments such as China's fear; they would also help counter the relentless rise in protectionist pressure in the West.

If emerging Asia needs a warning of the dangers of relying on exports, it need look no further than Japan. Japan's decade-long stagnation ended in 2002, thanks to a boom in exports, especially to China. Now, largely because of its failure to tackle the root causes of weak domestic demand, it is taking more of an economic hiding than any other rich country. Japan used to see itself as the lead goose in a regional flight formation, showing the way to export-led prosperity. It is time for the other geese to break ranks.

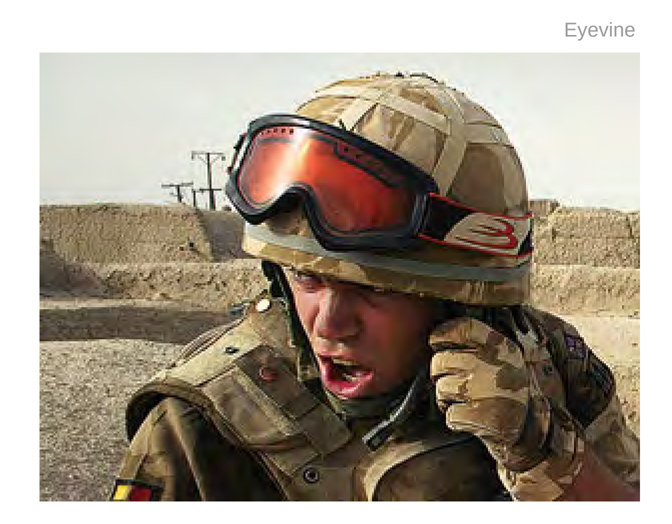
Britain's armed forces

Overstretched, overwhelmed and over there

Jan 29th 2009
From The Economist print edition

Seven years of war in Iraq and Afghanistan have exposed Britain's military failings. It can and must do better

Eyevine



EVERY year but one since the end of the second world war British soldiers have died in action in some corner of the world. Britain no longer has an empire, but it still does a lot of fighting and keeping the peace. Britons are proud of their armed forces. What makes them good is, in part, the experience of fighting and losing men, and they have certainly done a lot of both in Iraq and Afghanistan. But as well as hardening soldiers, wars expose military weaknesses. British forces are overstretched and have struggled to adapt to modern counter-insurgency campaigns. The country's most important allies, the Americans, are questioning Britain's commitment and military performance (see article).

Britain was seen to give up the fight in Iraq just as America acted to stem the bloodbath. British troops are due to leave Iraq this summer, but in Afghanistan the military effort is faltering. President Barack Obama sees Afghanistan as his military priority; he is likely to pour in more resources than George Bush did with the "surge" in Iraq. But British commanders say their forces are already under "unacceptable" strain.

The air force's transport fleet is in a poor state and the navy is shrinking, but the army is worst off. It was not designed to fight two protracted wars, and the strains are made worse by shortages of men and equipment. Battalions are up to one-fifth below their regular size; a further fifth or so are ill, injured or otherwise unfit to deploy. A multi-billion-pound hole in the budget for military equipment means new systems have to be scaled back, delayed or hollowed out. Buying kit is so expensive and takes so long that spending is out of kilter with current needs: most money now goes on fighter jets, aircraft carriers and submarines, which are of little use in Afghanistan. Good front-line equipment is being purchased with emergency funds, but there is too little of it to train with.

George Bernard Shaw once quipped that "the British soldier can stand up to anything except the British War Office." But bureaucrats are not the only ones to blame. The generals have failed to update their counter-insurgency doctrine and units still rotate every six months (American soldiers stay for 12). This leads to discontinuity and short-term thinking.

Power at a price

The withdrawal from Iraq will ease some of the pressures but not all. Britain needs to rethink its defence policy from the ground up; the last big review took place in 1998. The question is whether to increase defence spending, reallocate existing resources or scale back national ambitions; and that raises the deeper question of what kind of country Britain wants to be.

Like some European states, Britain could limit itself to defending its national territory while sheltering under NATO and America's nuclear umbrella. For an island nation, that would require only a modest navy and air force, and a small army. But for reasons mainly of history and pride, Britain has wanted to sit at the top table, to be a "force for good" in the world. It has seen its best chance of doing so in being America's closest friend, ready to take on a hard fight; and this role has won it not just diplomatic clout but also preferential access to intelligence and technology.

But being America's best military friend is an expensive business. It requires expeditionary capabilities—transport aircraft, field hospitals, aircraft carriers, deep-strike bombers—and, arguably, a nuclear deterrent. Among west Europeans, only France comes close.

Many maintain that Britain should give up the pretence of being a busy power. After the chaos in Iraq and the stalemate in Afghanistan, it is surely time to stop meddling in other countries, which only breeds resentment and more terrorism. As recession squeezes the budget back home, better to divert money from defence to tutoring poor children, developing green technologies—and bailing out banks.

Such arguments are tempting, but wrong. The Iraq invasion did raise Britain's profile among jihadists, but given its history in the Muslim world and its demographic links to Pakistan, Britain was anyway unlikely to avoid their wrath. Less martial countries too are in the terrorists' sights, to judge from the Madrid bombings in 2004, foiled plots in Germany and the attack on the Danish embassy in Pakistan last year.

Playing it safe

A direct military threat to Britain or NATO is unlikely but not impossible. A world in economic turmoil may well be more dangerous, not less so—as the spread of totalitarian ideologies in the 1930s suggests. Russia has gone to war with Georgia, uses oil and gas as a weapon, and sends its bombers buzzing close to Britain. Iran is probably building a nuclear bomb. In any case, defence policy is also about creating a more ordered world. The number of UN peacekeepers has grown sevenfold in a decade. Whatever the negative lessons of Iraq, intervention will sometimes be necessary to defend allies, stop mass killings, shore up fragile states, close down terrorist havens and relieve suffering. These jobs should not be left to America or to the poor states that contribute the most troops to the UN. Europe must do its share. The burden falls unfairly on countries that are willing to get involved. But without the lead given by Britain (and France), other Europeans would do even less.

If it is to maintain its troops' effectiveness, Britain will have to make some difficult choices. Like any form of insurance, defence policy must cover a range of risks: the safety of sea lanes is vital to move supplies in wartime and to trade in peacetime; supremacy of the skies is the prerequisite for success on land or sea. But Afghanistan is the priority, and although a lot more aid there would help, that war will be won or lost on the ground. The army needs more soldiers, helicopters and drones. If Britain cannot increase defence spending, then it must scale back less urgent projects, such as new fighter jets and aircraft carriers.

Abandoning Afghanistan, leaving a vacuum for the Taliban to fill, would mean a victory for extremism everywhere, a destabilised Pakistan and a less safe world. Losing today's war could make tomorrow's wars more likely.

Thailand

A sad slide backwards

Jan 29th 2009
From The Economist print edition

Witness Thailand’s disgraceful treatment of refugees, and much else


APCNN



LOCATED in a poor neighbourhood, Thailand is cautious about giving refugees a generous welcome. Doing so, it worries, might draw millions more across its borders, especially from Myanmar, a populous, wretched country with a ghastly regime. But there is no excuse for the astoundingly callous way Thailand has treated around 1,000 refugees from the Rohingyas, a Muslim minority group from Myanmar: beating them and casting them adrift on the seas without adequate supplies. Around 650 survivors have washed up in Indonesia and India in recent weeks; hundreds more may have drowned. This week Thailand was still dodging questions from the United Nations’ refugee agency about a further 126 Rohingyas whom the UN believes Thailand recently had in its custody but who may also have been dumped at sea.

The army, the source of so much other trouble in Thailand, is to blame. The Rohingya operation was overseen by ISOC, an army unit formed to fight communist insurgents during the cold war, whose powers were restored by the military-backed government that ran the country for 15 months after the 2006 coup. The army’s denials have been undercut by photographs obtained by CNN, showing soldiers towing rickety boats full of Rohingyas out to sea and cutting them loose.

Thailand’s new, fresh-faced, Oxford-educated prime minister, Abhisit Vejjajiva, says that the government will investigate the allegations against the army. But the army in effect put Mr Abhisit in power, when its chief orchestrated defections by a chunk of the previous governing coalition that had been led by allies of Thaksin Shinawatra, the prime minister whom the army pushed out in 2006. Mr Abhisit’s dependence on the generals means he is unlikely to be able to probe army misdeeds very thoroughly. The colonel alleged to have organised the dumping of refugees at sea is also accused of overseeing an atrocity against Muslims in Thailand’s strife-torn southern provinces in 2004. Amnesty International, a human-rights lobby group, accuses the Thai army of continuing to torture suspected Muslim insurgents in the south.

Not playing dominoes any more

There was a time, after the passing of its liberal 1997 constitution, when Thailand looked like becoming a role model for democracy and pluralism in Asia. The country’s elite still want it to be seen as a progressive, democratic country and a serious diplomatic actor. Unfortunately, in recent years it has slid backwards. This started with abuses by Mr Thaksin, followed by the army’s 2006 coup, and then the tacit backing that Queen Sirikit, some generals and Mr Abhisit’s Democrat party gave to thuggish anti-Thaksin protesters, one of whose leading sympathisers is Mr Abhisit’s foreign minister.

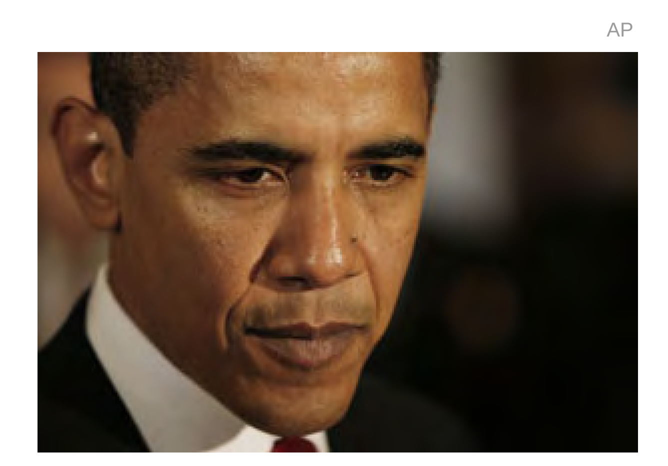
Yet, while soldiers act with impunity and royalist rioters get soft treatment, the country's anachronistic *lèse-majesté* law is enforced rigorously. America and its allies long turned a blind eye to such stains on Thailand's reputation, because King Bhumibol and his army were staunch anti-communist allies. Recalling that relationship, next month America is due to hold annual war games with regional allies in Thailand, a source of prestige for Thai generals. But the cold war is long over. President Barack Obama should threaten to move the games elsewhere until the Thai army is tamed. That would hurt the generals in their soft spot—their self-esteem—while doing little damage to America's interests or Thailand's people.

Brief encounter

Jan 29th 2009
From The Economist print edition

Barack Obama's bipartisan honeymoon has ended even sooner than anyone expected

AP



EVERY incoming American president promises that he will reach across the aisle. Senators and congressmen, Republican and Democrat alike, join in the hymn to the virtues of bipartisan effort. This time was no different: everyone applauded when Barack Obama said from the steps of the Capitol that "the stale political arguments that have consumed us for so long no longer apply." But, as usual, the stale political arguments have begun all over again.

Mr Obama set a cracking pace in his first days in office. He signed a lot of admirable orders, such as one closing Guantánamo within a year and others pushing for more fuel-efficient cars and ending the prohibition on sending aid to international organisations that provide abortion. He has buttered up the Republican minority in Congress, and they have gushed about how nice it is to work with him. Nonetheless, the first big partisan row of the new administration has already begun.

It concerns the new president's plans for the "American Recovery and Reinvestment Plan", the largest economic stimulus package ever devised: no less than $819 billion over the next two years in a bid to buoy up the shrinking economy and prevent the loss of millions of jobs. Many Republicans are worried about the hole this will make in the nation's accounts. They note that plenty of pork has crept into the bill, and that it will be impossible to spend that much that fast. It also contains some protectionist nasties in the shape of "Buy American" provisions. The bill, they say, is just a sneaky way of achieving standard Democratic big-government aims.

A bit rich, the Democrats retort, coming from the party that inherited a healthy surplus from Bill Clinton and turned it, thanks to tax cuts unmatched by savings, into a fair-sized deficit even before the recession began to bite. And besides, what else do the Republicans have to offer as a solution to the mess their president created? (Not very much, is the sad truth.)

Visible party lines

On January 28th the stimulus bill passed in the House of Representatives without a single Republican vote. In principle, that means that it could die in the Senate next week, since the Democrats are currently two votes short of a filibuster-proof majority there. That seems unlikely: the Republicans will not want to be blamed for the recession. But it signals an early end to bipartisanship and bodes ill for the future of more difficult legislation, which will require a lot more co-operation.

Whom to blame for the breakdown? The stimulus row apart, the Republicans can claim to have behaved

reasonably well, confirming Mr Obama's appointments without much fuss, though they did try, unsuccessfully, to vote down his new treasury secretary, Tim Geithner, for failing to pay his taxes on time. Mr Obama, for his part, has offered a lot of fine words about bipartisanship but has not produced very much of it, preferring instead to deliver on cherished Democratic aims. The same holds for the stimulus plan. True, the package contains a large dollop of tax cuts: some $275 billion of the $819 billion comes in this form. But most of that was proposed long ago by Mr Obama on the campaign trail, and so can hardly represent an attempt to forge post-election consensus. The Republicans have been given little say in drafting the plan, and the Democratic majority has taken advantage of the rules of procedure to frustrate their attempts to amend it.

On the other hand, Mr Obama has been careful to drop a few of the least stimulative and most contentious items. And no one doubts that some form of big stimulus is urgently needed. The Republicans could equally be accused of playing a cynical game, voting against a package they know will pass in order to appear thrifty yet not risk being accused of sabotage. In other words: it's politics as usual.

Broadband stimulus

Not so fast

Jan 29th 2009
From The Economist print edition

There is much talk about subsidies for high-speed broadband, but other causes are more deserving

Illustration by David Simonds



IN HIS first radio address as president, Barack Obama spoke of “expanding broadband to millions of Americans”. Britain’s prime minister, Gordon Brown, has likened his government’s efforts to extend the country’s digital infrastructure to “the roads and the bridges and the railways that were built in previous times” to stimulate the economy. Investing in broadband access sounds like a good way for governments to boost flagging economies. Digging up roads and laying all that optical fibre will create jobs; equipment-makers will have to crank out lots of new gear; and people for whom online commerce or remote working are today out of reach will be brought into the digital fold. One study suggests that increasing broadband penetration in a typical American state by a percentage point raises employment by 0.2-0.3% a year. The idea that governments should be pouring money into broadband seems so self-evident that operators and equipment-makers have been rubbing their hands with glee.

But as politicians announce their plans, they do not sound terribly ambitious. Mr Obama’s $819 billion stimulus package would make just $6 billion available for expanding broadband access—much less than expected, and with too many strings attached, grumble would-be recipients. In Britain, meanwhile, a plan to subsidise fast new fibre networks seems to have been ditched in favour of an initiative to ensure that broadband is available to anyone who is prepared to pay for it—in other words, filling in gaps in rural areas rather than boosting the speed of existing connections. So much for Mr Brown’s talk of a “communications revolution at a period when we want to stimulate the economy”, or Mr Obama’s campaign promise that “every American should have the highest form of broadband access”. Grand words have given way to puny deeds.

Campaigners and industry lobbies are livid. But the case for large-scale government investment in broadband is not as strong as its proponents claim. When it comes to promoting economic activity, it is easy to see why having broadband is better than not having it, but most benefits are likely to come from wiring people up in the first place rather than making existing connections hum faster. In Japan and South Korea over 40% of households have fibre links capable of blazing speeds, but that does not seem to have resulted in more rapid economic growth, or the emergence of new applications unavailable to consumers with ordinary broadband. So focusing on the extension of access into new areas is the right approach. Alas, that will not involve laboriously digging up lots of roads. Investing in, for instance, retrofitting buildings to make them more energy-efficient would create far more jobs.

Monopoly money

Another drawback with big state subsidies for broadband is that they could distort the market and create regulatory problems. Fibre networks are already being built by private companies in many countries; the prospect of handouts might cause them to delay their plans, in the hope that the state will pay for things they were going to do anyway. Weaker operators, unable to finance new networks, would certainly like governments to come to their aid. To ensure that governments do not end up creating new monopolies, it makes sense to insist that any firm that builds a network using state subsidies must also open it to rivals, unpopular though this is with those lobbying for aid.

Rolling out super-fast broadband for all, like motherhood and apple pie, is something that all politicians will claim to support. But when it comes to creating jobs and stimulating economic activity, it isn't the best use of government money.



On George Bush, bankruptcy laws, Brazil's border, lawsuits, Scotland, Helen Suzman, corporate jets

Jan 29th 2009
From The Economist print edition

Bush fire

SIR – The headline to your briefing on George Bush's legacy ("The frat boy ships out", January 17th) spoke volumes of the sneering, snarling disdain you hold for the man, which is so strong that it overwhelms your objectivity. The article was riddled with gratuitous swipes that were not backed up, such as "Mr Bush was the most partisan president in living memory". The only evidence you gave for this statement was a list of policies that were advocated by his party and which he pursued. Don't all presidents do the same? Where's the evidence that he did so more than other presidents? On the contrary, he also pushed several policies favoured by the Democrats, including new spending on entitlements and liberal immigration reform.

And I thought reforming America's entitlement system was something you supported? Mr Bush at least tried to revamp the public pension system. His desire to introduce private investment accounts wasn't just because the Republicans were enthusiastic about the "ownership society", it was also aimed at transforming Social Security into a sustainable programme.

Most of your enmity seems to be based on Mr Bush's Iraq policy, yet you made no mention of his main achievement and number one objective: keeping America safe after September 11th 2001. You let yourselves get sucked into the cult of animosity that materialised against George Bush. I pray you won't get caught up in the cult of personality that surrounds Barack Obama.

Patrick Chisholm
Chantilly, Virginia

SIR – There was little to argue with in your appraisal of the Bush years and the man himself. What is so deeply troubling is that you couldn't see this coming in 2000. Mr Bush came to that election with one of the most disturbing biographies of any candidate this past century—a man who incurred the wrath of his college professors as lazy and arrogant, a frat boy for sure, simplistic and indifferent to complex ideas.

He went on to become an alcoholic, business failure, a military no-show during the Vietnam war, a legacy candidate for state office, and a governor whose term in office was little more than a stage-managed prelude to running for president. And yet, based on your own fascination with his folksy ways and tissue-thin views on free markets, you endorsed him ("Crunch time", November 4th 2000).

If you had looked more closely at the man, the 2000 election, decided by the closest of margins, might have been different. I hold your esteemed newspaper as one of those most accountable for abetting the Bush tragedy of the past eight years.

Jack Luft
Sanibel, Florida

Europe's bankruptcy laws

SIR – I lead a hedge fund that focuses on investing in troubled businesses and distressed debt in Europe and I read your article on Europe's flawed insolvency laws with interest ("Out of pocket", January 3rd). I agree with your assessment that on the whole European insolvency laws are far from perfect and result in more liquidations than under Chapter 11 of America's bankruptcy code. However, European laws have improved significantly over the past few years. The statistics you cited on creditor recovery are indicative neither of the improvement in the laws nor of their quality as there have been relatively few European insolvencies in that time, and those businesses that have filed have been either the weakest of the weak

or fraudulent.

Moreover, Chapter 11 is a mixed blessing because it allows management teams to control the in-court process to facilitate reorganisation, which means a vast amount of the debtor's estate is spent on professional fees and other costs (as epitomised by Enron and Adelphia). In practice, the fact that management teams in Europe typically lose control of the in-court process means they have an incentive to come to the negotiating table with creditors to secure out-of-court restructuring earlier than in America, often avoiding the time and costs associated with a formal insolvency process.

Timothy Babich
Managing partner
Fortelus Capital Management
London

Plugging Brazil's border gap

SIR – As well as exerting influence in foreign affairs and policing the Amazon, there is a more immediate reason for increasing the size of the Brazilian army ("But what is it for?", January 17th). The Brazil-Paraguay border is vast, largely uninhabited and poorly patrolled and is the point of entry for many of the illegal arms smuggled into Brazil that end up in the hands of gangs in the coastal cities. Strengthening Brazil's army at this border may be just as important to protecting lives and safeguarding national interests as expanding its presence anywhere else in Brazil or abroad.

Eliot Brockner
New York

Not really lovin' it

SIR – Lexington suggested that the case in which a woman sued McDonald's "for serving her the coffee with which she scalded herself" is an example of the "nuttiest" kind of lawsuit (January 17th). I think this is misleading. McDonald's chose to keep its coffee hotter than that of its rivals. This choice exposed customers to the unexpected danger of being scalded. My coffee machine at home produces a brew at a temperature I can drink immediately, with no risk of harm should I spill it on myself. Far from being an example of a frivolous suit, the McDonald's case is actually an example of how the current tort system protects the public from corporate misdeeds.

Tim Jordan
Charlotte, North Carolina

SIR – The woman in question, Stella Liebeck, suffered third-degree burns over 6% of her body. She offered to settle for her medical costs ($20,000) but McDonald's refused even though they knew from some 700 previous reports about the dangers of their plus-80ºC coffee. Other fast-food restaurants serve their coffee at less than 70ºC.

James McCrostie
Kawagoe, Japan

Brave heart

SIR – It comes as no surprise to the millions of people of Scottish extraction living in England that more Burns night suppers take place here than in Scotland ("Selling Scotland by the verse", January 24th). We must surely outnumber Scotland's resident population. You also mentioned that Scotland's first minister, Alex Salmond, has designated 2009 as a "Year of Homecoming". We are touched by this, especially as he wants a referendum to undo the union and to make Scotland a foreign country to us. In effect, this would render us stateless. We now await word from Mr Salmond that his offer of homecoming is sincere, and that we will be allowed to vote in any referendum on the issue.

A.J. Lane
East Grinstead, Sussex

Political backbone

SIR – Helen Suzman had a remarkable acid wit (Obituary, January 10th). After a particularly loathsome piece of security legislation was passed in South Africa's Parliament with the unanimous support of the now defunct and toothless United Party, she said she glanced at the opposition benches and saw a shiver running around looking for a spine to run up.

Peter Surtees
Sun Valley, South Africa

The following letters appear online only

Suffer a jet

SIR – I read your article about companies putting their corporate jets up for sale ("Deeply uncool", January 10th). I would argue that with the world economy the way it is and with markets as flat as they are, now is the perfect time to own or use a business aircraft. Big companies are under fire for operating their own aircraft. The general consensus seems to be that they are merely a perk for overpaid, undeserving bosses that enable them to fly to their private islands and family ski retreats. Little is ever said about the fact that most business aircraft are undeniably the best and often only way for executives to maximise their productivity by attending meetings at various destinations within the course of one or two days in order to sign contracts and develop new business.

Such destinations are often not adequately served by commercial airlines, and seldom with schedules that meet business needs. In the face of airline consolidation and declining service, including the cancellation of routes at short notice and interrupted schedules, business aviation is now being seen for what it truly is: a significant tool for growth.

Moreover, business aviation can help the wider economy as well. We recently released a report compiled by PricewaterhouseCoopers that showed the business-aviation sector contributing a total of €19.7 billion ($27 billion) in annual gross value added to the European economy in 2007; this accounted for approximately 0.2% of the combined GDP of the European Union, Norway and Switzerland.

Don't damn corporate jets as a luxury or leave them in the hangar wasting money. Use them now as the essential tool they are to re-establish business and build the foundations of recovery.

Eric Mandemaker
Chief executive
European Business Aviation Association
Brussels

SIR – The statistics on the use of corporate jets are extraordinary. More than 70% of the time the aircraft fly with one or two people as passengers and they often fly empty after dropping someone off or picking someone up. To add insult to injury, corporate aircraft utilise the same resources that commercial aircraft use. The resources required of the air-traffic control and airport system to fly a chief executive in his jet are the same required to fly a 767 full of passengers. Corporate jets further clog up our already crowded airspace.

Business aviation is a boondoggle. Often such travel and corporate expenses are buried deep within financial statements and hard for shareholders to quantify. Granted, there are some corporate flight departments that are efficient and cost-effective, but they are few and far between. It is time for both shareholders and taxpayers to assess the value of such conveniences for the well-to-do.

Frank Ketcham
Sausalito, California

Economist.com BRIEFINGS

China's economy

A great migration into the unknown

Jan 29th 2009 | XINJI
From The Economist print edition

Global recession is hitting China’s workers hard

Getty Images



AS THE lunar new year holiday winds down in China, millions of workers are expected to stream back from the countryside to jobs in the cities. But in Xinji, a fur- and leather-processing city in northern China and a big producer of holiday fireworks, there will be little to go back to. The global economic crisis has dealt a hefty blow to this once booming city.

China’s leaders are struggling to cope with the biggest upsurge of unemployment the country has faced in years. Migrants from the countryside, the main source of labour for export-oriented industries and construction sites, have been the hardest hit so far. Millions have been thrown out of work. Urban white-collar workers, for years pampered by double-digit growth, speak of shrinking bonuses and frozen wages. Some are losing jobs, too. Students, whom the government always fears upsetting, face the most difficult employment prospects since the upheaval in Tiananmen Square 20 years ago. As the Communist Party prepares to celebrate 60 years in power on October 1st, it worries that citizens will be in a fractious mood.

Xinji sits about four hours’ drive south of Beijing, in the dusty plain of Hebei province. It is typical of China’s many fast-emerging cities, driven by the big ambitions of local governments. It is now just as typical of the many Chinese boomtowns that are hitting the buffers. Xinji has suffered badly from falling demand for its clothing exports. By November, most of its factories had closed two months earlier than normal for the spring festival break. Tens of thousands of workers went back to their nearby villages, expecting to return after the holiday. Many won’t do so.

This is a huge problem for Xinji’s government, whose aspirations are symbolised by the city’s new town with its broad boulevards, an Eiffel-Tower-like structure at one crossroads and a rocket-shaped protrusion on top of the leather-clothing exhibition centre. It had been planning for an average of 13% growth a year for the rest of the decade. When thousands of Chinese factories began to halt production late last year as export orders dried up, much attention focused on the travails of Guangdong, an export-driven southern province bordering on Hong Kong. Several protests broke out as factories there closed down, leaving employees unpaid. But after making their point, many of the workers departed for their home villages in distant inland provinces. Xinji’s workers are mainly local. It cannot shed its difficulties so easily.

Nor can many other towns and cities across China. Figures relating to the country’s migrant labour force are vague. But officials believe that of more than 200m non-agricultural workers from the countryside, more than 80m work close to their villages.

The proportion working closer to home has increased in recent years, as more jobs have appeared inland that offer better conditions than factory work in Guangdong and other places on the coast.

In Maoying village on the edge of Xinji, next to a leather-processing zone, the Communist Party chief, Li Qiangbao, says 400 villagers would normally be employed in nearby factories. Mr Li says he thinks many of them will still be able to find at least some work after the holiday, but they will be earning less. This may be over-optimistic. Marc Blecher of Oberlin College says Xinji is a good example of “market Leninism” in China. Its government-inspired focus mainly on one line of business helped it prosper, but may be its undoing.

In the early 1990s local leaders decided that Xinji’s future lay in leather and fur. They compelled the area’s widely scattered village-run tanneries to consolidate and move to new industrial zones where, supposedly, they could enjoy economies of scale and control pollution better. They established a huge leather and fur-trading centre and encouraged entrepreneurs to look abroad for markets.

Most of Xinji’s fur and leather exports ended up in the former Soviet Union, Russia in particular. To get around slow and cumbersome customs procedures, most Xinji exporters hired Russian middlemen with government connections to speed things up. Officials worried about this capricious system and an over-reliance on Russia, but quality was not quite good enough for a big push into Western markets. The city prospered anyway. By its own reckoning, Xinji’s economy grew by 13.4% in 2007 (close to the national rate), with leather and fur products making up about 80% of its exports of more than $200m. Until the global crisis hit, around 80% of these products were sold abroad.

“Protect Eight”

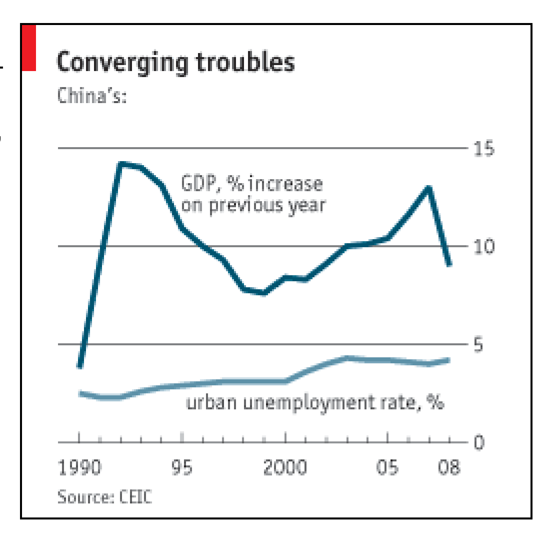
Chinese officials—Xinji’s included—often proclaim that high growth is crucial for social stability. They say that 8% is the minimum needed to prevent joblessness from triggering serious unrest (more serious, that is, than the tens of thousands of mostly small protests that occur every year in China, even at the best of times). The figure may be arbitrary, but the frequent repetition of the “Protect Eight” mantra sends a clear signal to local authorities that they cannot afford to slacken. Most of them have aimed for, and achieved, much higher targets in this decade.

The governments of Xinji and many towns like it must now be worried. Early this month Xinji’s party chief, Zhang Guoliang, told a gathering of senior officials that maintaining high growth remained “an unshirkable task”. But he lowered his sights. In 2009, he said, Xinji would strive for 10% GDP growth along with an 8% increase in farmers’ net incomes and an 11% rise in urban disposable incomes. In a city of idle or semi-idle factories, this still sounds ambitious. In the past Xinji has found it hard to benefit from export-tax rebates, such as those announced by the central government late last year in an effort to revive labour-intensive industries. Because of the dodgy methods used to ship goods to Russia, there are no receipts for claiming the rebates.

China’s system of residential registration, a legacy of the Mao era that divides citizens into urban and rural according to their parentage, means that workers from villages around Xinji who work in the city’s leather factories remain, technically, farmers. Their wages are therefore counted in the farmers’ net income category. (Xinji, like all Chinese cities, includes an urban area and a much larger rural hinterland. Its official urban population, including “farmers” who have stayed longer than six months, is around 200,000. More than 400,000 live in the countryside.) This makes Mr Zhang’s income-boosting goal an especially tough one. About a third of the income of Xinji’s “farmers” derives from the leather industry. In Maoying village around two-thirds comes from leather and other non-farming work.

Zhang Jianmin, of Minzu University in Beijing, reckons that

around 10% of Chinese workers from the countryside who are employed beyond their home areas will be out of a job this year—about 15m people. Officials have little idea what will happen to them. Many, they hope, will scatter across the countryside where, though disaffected, they will at least have food and shelter. Another Maoist legacy is the entitlement of those classified as rural dwellers to the use of a piece of land. It is usually tiny, but big enough to live on.



In recent years, however, millions of farmers have lost all their land to relentless urban expansion (local governments have profited massively from selling appropriated rural land to developers). Many of these farmers have been absorbed into the urban workforce, but often not into urban social-security schemes. They face a perilous future. Millions of jobless migrants may well remain in cities, if not protesting then at least pushing up crime rates.

The central government is anxious to cushion the blow. It has made it easier for farmers to register new businesses and has encouraged banks to lend them money. Local authorities say they are providing free job training for returning migrants. President Hu Jintao has just announced big increases this year in agricultural subsidies.

But there are reasons to be sceptical. Few rural folk may be keen to start new businesses during a slowdown, even if the state-owned banks are willing to lend to them (most farmers have little to use as collateral, since their land-use rights cannot be mortgaged). Local governments in poorer provinces, where most migrant workers come from, may well balk at spending more money on training at a time when their revenues are falling. One Chinese newspaper said boosting grain subsidies would probably be offset by the continuing high cost of fertiliser.

In Maoying village a poster announces a plan to boost benefits for participants in a new rural health-care scheme, which has been rolled out across the country over the past few years. Yang Lianyun of the Hebei Academy of Social Sciences says that government subsidies for this scheme have increased by 50% this year in Shijiazhuang prefecture, to which Xinji belongs. But the impact of this may also be less than meets the eye. Even with such increases, rural residents still have to pay a large part of hospitalisation costs out of their own pockets. Some prefer not to go. On top of a 4 trillion yuan ($585 billion) stimulus package announced in November, the government said on January 21st that it would spend 850 billion yuan on extending health insurance to more than 90% of citizens over the next three years. But details of both plans have yet to be announced.

Barber-shop discontents

The government has some grounds for hoping that it can weather the rural storm. Vague and incomplete government statistics suggest that protests have been rising generally in China in recent years. Most of them have occurred in rural areas, often as a result of land seizures. In a barber shop in Maoying, customers fume about pollution and local corruption (sentiments echoed on local internet forums). But protests have been directed against local governments and have not explicitly challenged the Communist Party's monopoly of power. There is also little sign of co-ordination among different disaffected groups.

With some notable exceptions, the party is getting better at handling unrest. In Hebei province the authorities are keen to maintain social calm, since the province surrounds the capital as well as the port city of Tianjin. Directives on dealing with "sudden incidents", issued by Xinji last year, repeat the central government's constant slogan that "stability is paramount". They stress the need to placate protesters rather than respond with force.

Rural China is no stranger to sharp employment fluctuations. In 2003, during an outbreak of SARS, many migrant workers were forced to return to their villages for several weeks. Migrants in and around Beijing also experienced severe disruption before and during the Olympic games in August last year, when the government ordered the temporary closure of many dirty industries and restricted movement to the capital. Neither episode triggered serious unrest, despite the blow to incomes.

In the late 1990s, even amid the Asian financial crisis of 1997-98, China resolutely carried out a massive

restructuring of its state-owned enterprises (SOEs). Some 40m lost their jobs. As many people lost their jobs each year as the number forecast for migrant labourers this year. It was traumatic for those involved, who (unlike today's migrant workers) believed that they enjoyed jobs for life. Protests were frequent; some, in the rustbelt of the north-east in 2002, were the largest China had experienced in many years. The unrest was urban, close to seats of party power and embarrassing to a party that prided itself on being the champion of the proletariat. Yet, apart from an adjustment of party rhetoric that year towards a more pro-poor line, the political fallout was minimal.

But there are important differences between then and now. For one thing, the SOE restructuring hit blue-collar workers hard even as the middle class—a new pillar of support for the party—was beginning to grow and flourish. At the same time as closing down, selling off and merging SOEs, the government virtually gave away the housing stock attached to them. This ensured that laid-off workers still had somewhere affordable to live (they also got subsistence payments that today's migrants would envy). And it gave the new middle class an asset base that would soar in value—until, that is, the deflation of China's property bubble last year and the onset of the current crisis.

Restless citizens, dangerous students

Now the party faces broader discontent. China's notoriously contentious unemployment figures, which do not cover migrant workers (no statistics are published for rural joblessness), look rosy beside those of some Western countries. But they suggest a growing problem. On January 20th the government said the urban unemployment rate in 2008 rose to 4.2%, up from 4% the previous year and the first increase in five years. The government's target for this year is to keep the rate below 4.6%—the highest figure since 1980.

EPA



Idle graduates find a new occupation

In Xinji it is the relatively pampered urban workforce (by official classification) that has been the first to break ranks. For three days, beginning on January 8th, as many as 300 workers from the Xinji Spinning and Weaving Company gathered outside the city government's headquarters to demand the subsistence wages promised by their employers when the former state-owned factory closed in August.

Since the SOE reforms a decade ago, the internet has become a far more widely used and powerful medium for dissent. Protesters in Xinji used it to draw attention to their complaints. Many citizens wrote messages on a local bulletin board expressing their support. One of Xinji's deputy mayors met the demonstrators and helped to arrange payment of the overdue money, possibly (some say) with government funds. Buying protesters' silence is a frequent tactic of local officials, who fear that visible unrest may tarnish their careers.

Among urban citizens, it is the job prospects of graduates that worry officials most. A rapid increase in the number of university places in recent years has been accompanied by declining numbers of college leavers who regard themselves as suitably employed. A record 5.6m graduated last year, nearly 650,000 more than the year before. Another 6.1m will graduate in 2009. Around 1.5m, however, were jobless at the end of last year. This month China's prime minister, Wen Jiabao, convened a cabinet meeting to discuss the problem ("If you are worried, I am more worried than you," he had told students during a campus visit earlier). The government said it would give loans to graduates to help them start businesses as well as to companies that employ them.

Discontent among students is particularly alarming to Chinese officials because of the historical role they

have played in political upheavals, from the anarchic Cultural Revolution in the late 1960s to the Tiananmen Square protests of 1989. The authorities will be particularly vigilant around May 4th, the 90th anniversary of student-led protests that led to the birth of the communist movement, and on June 4th, the 20th anniversary of the suppression of nationwide student demonstrations calling for more democracy. The students involved in the 1989 unrest were also disheartened by grim job prospects.

But there has been little sign of political activism among students in recent years. They have taken to the streets only to make nationalist points, and in support of the government. The authorities worry about the destabilising potential of nationalist ferment too, but far less than it does about calls for democratic reform.

Whether or not unemployment brings unrest on the scale seen in 1989, the party will be severely challenged over the next few months. Disagreement is growing within its own ranks, and between different parts of the bureaucracy, over how to spend the money earmarked for stimulus measures and how to prevent it being siphoned off, or pocketed, by local governments. President Hu and Mr Wen will face considerable pressure to do more to help farmers and the urban poor. Just before the lunar new year the government announced unprecedented one-off payments totalling 9.7 billion yuan to 74m people living close to the poverty line. President Hu also sought to burnish his political credentials by visiting Jinggangshan, an area known as the cradle of the Chinese communist revolution.

In January 2008 a law was implemented that made it harder to fire employees. Now some complain that it is being widely ignored. Other laws are being stretched, too. In December Xinji's environmental bureau said that in order to "address the negative impact" of the crisis, it would "simplify" procedures in order to provide swift clearance for those projects that would create "little" or no pollution—a strong hint that it was lowering its guard.

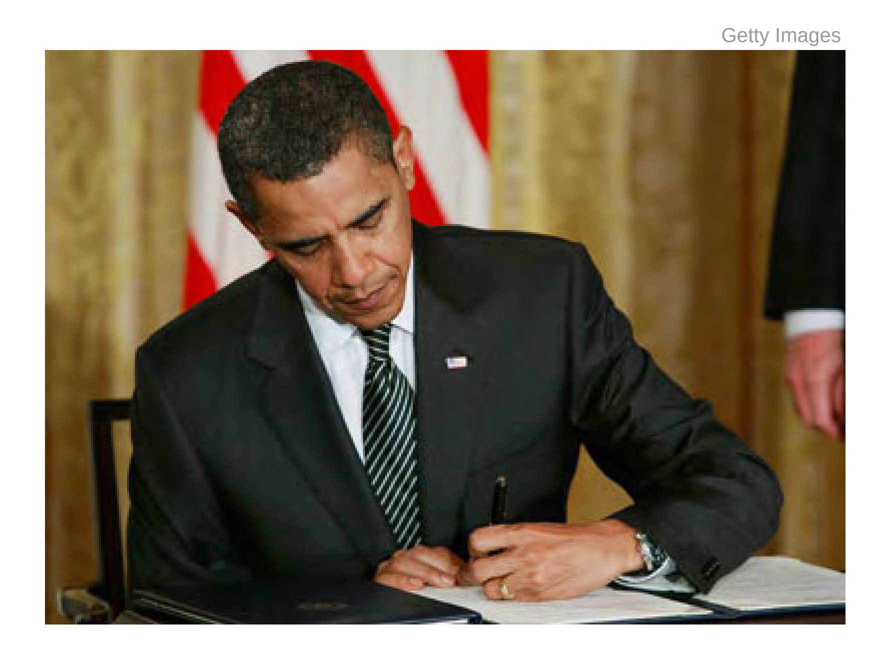
Wu Xiaoling, a former vice governor of the central bank and now a senior legislator, is said to have suggested recently that GDP growth should cease to be used to judge officials' performance. Improving "public welfare" should instead be given top priority, she said. Messrs Hu and Wen want to keep both the pro-growth and the pro-welfare camps happy (more welfare spending, they reckon, could help consumers to save less and spend more). But most of all they want local governments to keep factories and businesses open.

Barack Obama's start

High hopes, horrendous workload

Jan 29th 2009 | WASHINGTON, DC
From The Economist print edition

Getty Images



America's new president has started at a sprint. But it's an obstacle course

THE party is over. The crowds have gone. The empty tubs of Ben and Jerry's “Yes, Pecan” ice cream have been binned. Shops are selling “And He Shall Be Called Barack Obama” T-shirts at a generous discount.

But before the new president has got comfortable in the Oval Office, he has been buffeted by bad economic news. American firms announced at least 65,000 job cuts on January 26th alone. Unemployment, which was 4.9% only a year ago, stood at 7.2% in December and is sure to rise. The only bright news was that house sales rose 6.5% between November and December, as buyers snapped up bargains.

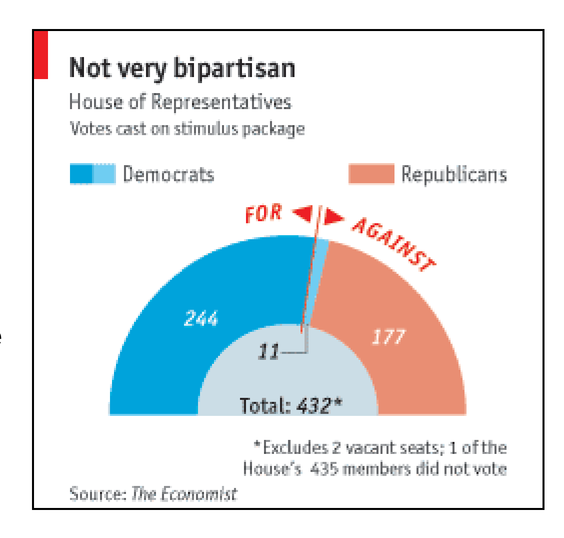
Mr Obama spent much of his first week trying to push his gargantuan stimulus package through Congress. The package includes some $275 billion in tax cuts and handouts and $300 billion in short-term spending, such as aid to cash-strapped states for providing health care, unemployment benefits and so forth. The Congressional Budget Office, a non-partisan number-cruncher, reckons about two-thirds of the package could be pumped into the economy within 19 months. That should help soften the recession.

The rest of the package, however, consists of longer-term investments in infrastructure, such as $50 billion to promote energy efficiency and alternative energy, $30 billion for roads and bridges and $20 billion for computerising health care. Mr Obama sees these expenditures as a first step towards more radical reforms. Some Democrats think he does not go far enough; that he should take advantage of the crisis to push a big shake-up of health care, energy and transport straight away. Others think he should pursue the short-term stimulus quickly but take his time over long-term plans and get them right.

Republicans agree on the need for short-term stimulus, but want it to consist largely of tax cuts. House Republicans have proposed an alternative package including a 5% income-tax cut, a freeze on dividend and capital-gains taxes and a hefty increase in the deductions families can claim for children. Mr Obama met House and Senate Republicans on January 27th. But many Democrats feel he has already conceded enough by allowing so many tax cuts in his own proposal.

On January 28th the House of Representatives gave Mr Obama what he wanted, passing an $819 billion package. The bill passed comfortably by 244 votes to 188. But not a single Republican

supported it. Much of the padding that Republicans had so vociferously objected to, such as a proposal to buy fleets of new government cars, stayed in. The bill now goes to the Senate, which is expected to make it even larger. Senate Republicans could block it but probably won't. They don't want to be blamed for the recession.



Meanwhile, Mr Obama's economic team is struggling to find the best way to prop up the financial sector. Many financial institutions are tottering under the weight of toxic securities. The original plan, hatched under George Bush, was that the government should buy up these assets. But if it buys them at market prices, which are horribly depressed, other banks will have to write down the value of similar assets on their books, which could trigger more trouble. The government could buy the assets at above-market rates; but that would be expensive and unpopular.

Mr Obama won an early victory when the Senate confirmed his treasury secretary on January 26th. Tim Geithner, who helped shape last year's financial bail-out, is deemed knowledgeable and competent. But he failed to pay a big chunk of his taxes on time. Mr Geithner also upset the Chinese government by saying that Mr Obama thinks it manipulates its currency. But he was careful to add that America should not start a trade war over this.

Other confirmation hearings have gone more smoothly. Hillary Clinton was confirmed as secretary of state by 94 votes to two. Six other cabinet members were approved without objections, including Janet Napolitano for homeland security, Steven Chu (energy), Arne Duncan (education) and Ken Salazar (interior).

Virtuously, Mr Obama announced that no lobbyists would serve in his administration. Embarrassingly, he had to waive the rule immediately for two of his team. William Lynn, a lobbyist for Raytheon, a firm that makes missiles, is to be deputy defence secretary. And William Corr, a former lobbyist for an anti-smoking group, is to have a top job at the health department.

On January 22nd Mr Obama ordered that the prison at Guantánamo Bay be closed within a year. But he has not decided what to do with the prisoners there, some of whom are thought too dangerous to free (see article).

He appointed an envoy to South-West Asia (ie, Afghanistan and Pakistan): Richard Holbrooke, a veteran diplomat. And he named another envoy to seek peace between the Israelis and the Palestinians: George Mitchell, a former Senate majority leader who helped broker peace in Northern Ireland. Mr Obama sent Mr Mitchell immediately to the Middle East, and told an Arabic news channel that he plans to "start by listening, because all too often the United States starts by dictating."

But Mr Obama has fists as well as ears. Three days after his inauguration, missiles apparently fired from American drones killed eight suspected foreign terrorists in Pakistan, and more than a dozen civilians. Such attacks are unpopular with Pakistanis. Following Mr Bush's practice, Mr Obama made no comment about them.

Meanwhile the defence secretary, Robert Gates, said that Mr Obama's plan to double American forces in Afghanistan would probably lead to higher casualties. And Iran's president, Mahmoud Ahmadinejad, soured the global welcome party by declaring that "Change means giving up support for the rootless, uncivilised, fabricated, murdering...Zionists."

Without fanfare, Mr Obama lifted a ban—regularly imposed by Republican presidents—on American aid money going to charities that provide abortion. To please environmentalists, he ordered the Environmental Protection Agency to consider letting California set its own emissions standards (ie, stricter ones) for cars. And his State Department appointed an envoy, Todd Stern, to discuss climate change with other countries.

No one doubts that Mr Obama can walk on water. (Washington was frozen over this week.) But he will have a tough job doing everything he says he will, even assuming that China keeps lending him the money to do it. His second week will doubtless be equally frenetic. And he still has a budget to deliver

next month.

Guantánamo

Promises to keep

Jan 29th 2009
From The Economist print edition

And an oath to uphold

AP



Where to now?

NO ONE will hear President Barack Obama let slip the words “war on terror”. His decision to close the Guantánamo Bay prison camp within a year was intended to draw a clear line for all to see between George Bush’s efforts to consign foreign terrorist suspects to legal limbo and his own vow to restore America’s commitment to the rule of law. But Mr Obama still has to decide what to do not just with Mr Bush’s captives, but with any picked up on his own watch. He took an oath to keep America safe as well as free. After the applause for his Guantánamo decision, it emerged that he had left himself lots of room to work out how.

The devil—and the disappointment for some—will be in the detail of other directives signed last week. Officials have 180 days to come up with “lawful” options for dealing with detainees, and just 30 days to ensure that all those held in American custody anywhere are treated humanely. They also have 180 days to decide whether the CIA needs, as some insist, to be able to use harsher interrogation techniques (still short, presumably, of unlawful torture) than are allowed in the Army Field Manual. Until then, the manual is law.

Mr Obama knows that America will need a way to keep dangerous terrorist suspects off the streets, however well their jailers treat them. Of the 800 or so who have passed through Guantánamo since it opened in 2001, 242 are still stuck there.

The number can be whittled down. Countries from Britain to Saudi Arabia have already taken back nationals or residents, including some potentially dangerous characters. Mr Bush had been pressing others to take in the roughly 60 who, though cleared for release, could not be sent home; an expedited review of cases will have Mr Obama pressing harder. Reports that at least 61 of the more than 500 detainees freed from Guantánamo thus far have reverted to violence will not help.

Finding those “lawful” solutions for the too-dangerous-to-release lot will be even trickier. Human-rights campaigners want them to have their day in court—federal district court, tried under criminal law. Federal courts have a good record in trying terrorism cases, says a recent report by the Centre for Strategic and International Studies, a think-tank. But even with “clean teams” collecting fresh evidence, untainted by accusations of past harsh treatment, few cases may go to trial this way; even where suspects were nabbed properly, especially in conflict zones, FBI-standard evidence-collection was not a priority.

Those deemed ordinary fighters, such as Taliban picked up on battlefields in Afghanistan, could be held legally as prisoners-of-war until hostilities have ended. But in many cases standard laws of war may be

too hard or too risky to apply: to those whose proper identities are unknown, for example, or who are suspected of loyalty not to tribal commanders but to al-Qaeda's network of terrorist affiliates.

The solution, argues Ben Wittes of the Brookings Institution, another think-tank, is for Congress and the administration to devise a properly constituted, accountable detention system, one designed to protect sensitive information that can nonetheless be challenged by defence lawyers. A line under the past still, but not quite so clear.

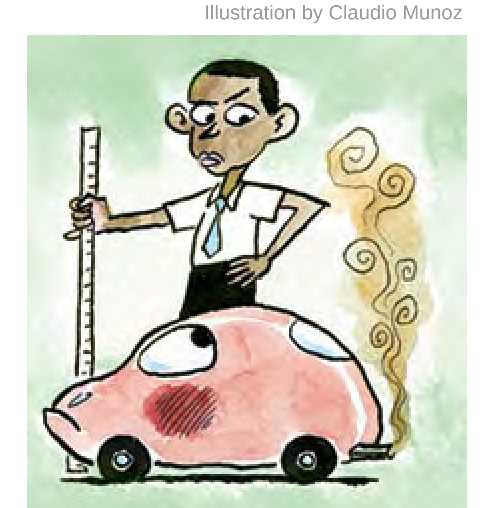
Greenhouse-gas emissions

California's green light

Jan 29th 2009
From The Economist print edition

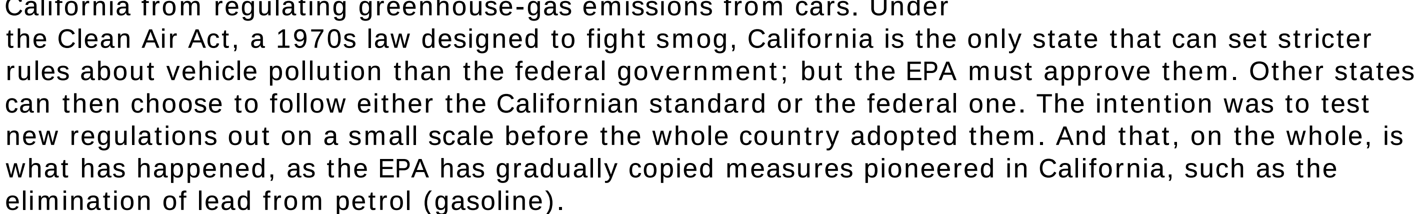
The president directs the EPA to reconsider standards

Illustration by Claudio Munoz



AS A senator, during his campaign for the presidency and in his inaugural address, Barack Obama repeatedly pledged to reduce America's dependence on foreign oil and to tackle global warming. On January 26th he made what he called "a down-payment" on those pledges, signing two executive orders concerning greenhouse-gas emissions. The move signalled a break with George Bush's foot-dragging and hinted at grander things to come.

The first order instructed officials to come up with a federal fuel-economy target for 2011. Mr Bush had signed a bill in 2007 that will require much more abstemious cars by 2020, but then dallied over its implementation. Mr Obama's edict will reinstate some zeal.



The second order is more momentous. It instructed the Environmental Protection Agency (EPA) to reconsider its decision last year to bar California from regulating greenhouse-gas emissions from cars. Under the Clean Air Act, a 1970s law designed to fight smog, California is the only state that can set stricter rules about vehicle pollution than the federal government; but the EPA must approve them. Other states can then choose to follow either the Californian standard or the federal one. The intention was to test new regulations out on a small scale before the whole country adopted them. And that, on the whole, is what has happened, as the EPA has gradually copied measures pioneered in California, such as the elimination of lead from petrol (gasoline).

In 2002, the state passed a law obliging carmakers to reduce their vehicles' greenhouse-gas emissions by 30% by 2016. In effect, that would require them to improve fuel economy roughly twice as fast as the federal government's bill, since the only straightforward way to reduce emissions is to increase efficiency. But the EPA under Mr Bush rejected the law, despite a ruling from the Supreme Court that the Clean Air Act could be applied to greenhouse gases.

The new administration's blessing looks certain. The EPA's new boss, Lisa Jackson, has already said that she is inclined to give California the go-ahead. Since another 13 states follow California's standards, they could soon apply to almost 40% of the national market for cars. America's previously hostile carmakers greeted the order meekly, doubtless mindful of their new-found dependence on the government's generosity.

Mr Obama has said that he would like Congress to pass a comprehensive law on climate change. But the orders serve as a reminder that the president's existing authority on the subject is quite broad, and suggest a willingness on his part to use it. That might help focus minds on Capitol Hill. For every down-payment, after all, there is a balance outstanding.

Trade policy

Buying American

Jan 29th 2009 | WASHINGTON, DC
From The Economist print edition

Economic nationalism rears its ugly head

IN 1929 Willis Hawley and Reed Smoot, two protectionist Republicans in Congress, sponsored a bill to raise tariffs to the highest levels America had ever seen. And in the midst of economic distress, the protectionists won. The result was a round of reciprocal tariff hikes elsewhere, and a disastrous collapse in international trade.

This was exactly the sort of thing the ministers of the G20 sought to avoid when they met in Washington late last year, agreeing not to devise new trade barriers as the world economy fizzles. But the Democrats are doing just that, anyhow, in the stimulus bill currently winding its way through Congress.

House Democrats want to require that all iron and steel used in stimulus-funded infrastructure projects should be made in the United States. America's steel producers are happy, especially since they saw their share of the world steel market fall from 7.9% to 7.2% in 2008. But American exporters fear retaliation against their goods, both in places like China, at whom the steel provisions are aimed, and in rich countries, which are already slipping domestic-purchasing requirements into their own stimulus packages (see article).

The House favours another so-called "Buy American" requirement for spending on uniforms for the more than 100,000 officers in the Department of Homeland Security. And, though it is not in the House stimulus bill, some lawmakers still favour directing the $20 billion that is being allocated for computerising medical records exclusively towards American tech firms. Such a requirement, they say, is justified in an economic-stimulus package. But critics point out that it is hardly possible to meet it (IT being such a global business), even if it were a good idea.

Such naked protectionism may violate international trade rules. But another perverse idea floating around Capitol Hill is to limit stimulus-related purchases to countries that have signed the World Trade Organisation's agreement on government procurement. A treaty set up to encourage non-discrimination in government purchases would thus be twisted to bar the American government from buying goods from countries such as China and India.

Before Mr Obama became president, the consensus was that the ascendant Democrats would merely drag their feet on trade matters. But the huge sweep of the stimulus bill has overshadowed its elements, such as Buy American provisions. So they may yet sneak through.

Ambitions are high. Tim Murphy, a Pennsylvania congressman, is championing a bill that would give Congress power to review presidential decisions on whether or not to increase import duties in the face of sudden dislocations. Not Smoot-Hawley, but still worrying.

New York and Illinois

Over-mighty governors

Jan 29th 2009 | NEW YORK
From The Economist print edition

It’s time to curb their power to pick senators

AP



Not sweet enough, Caroline

WHEN David Paterson unexpectedly became governor of New York last year after Eliot Spitzer’s resignation, he impressed everyone by putting the economic crisis before politics. He was doing rather well until he had to appoint someone to fill the Senate vacancy left by Hillary Clinton when she was made secretary of state.

Caroline Kennedy, John Kennedy’s daughter, wanted the job. As an early supporter of Barack Obama, she would have had his ear. Though lacking any political experience (she left the White House when she was six), she would at least have been an excellent fund-raiser for the Democratic Party and Mr Paterson in particular. But Ms Kennedy stumbled from the start. She lacked political charisma and failed to explain her views on important issues. Her apparent sense of entitlement annoyed many, including—some said—the governor. And polls revealed that New Yorkers did not want her anyway. Ms Kennedy withdrew from the process on January 21st for “personal reasons”. The speculation has been intense, but inconclusive.

Mr Paterson’s two-month selection process was needlessly drawn-out. His tendency to gossip about it was distasteful. A Paterson staffer reportedly made anonymous malicious remarks about Ms Kennedy to the press. Michael Bloomberg, New York City’s mayor, called it “cheap, dirty politics”. Mr Paterson tried to undo the damage but ended up making things worse.

His eventual choice was a surprise. He appointed Kirsten Gillibrand, a “blue dog” Democratic congressman from upstate New York, who had just been re-elected to her second two-year term. He must be hoping her more conservative base will help him in his 2010 campaign. She is supported by the National Rifle Association and is perceived to be anti-immigrant, neither of which endears her to liberal Manhattanites. “She took positions that reflect her constituents,” says Gerald Benjamin, of the State University of New York.

Illinois’s adventures in patronage have been even more disastrous. Rod Blagojevich, a man most people would no longer trust to appoint a dog catcher, has the right to choose Mr Obama’s successor in the Senate. After he was accused of plotting to sell the Senate seat, there was talk of a special election. But Democratic leaders in Springfield, the capital, stalled, and the result was that the governor’s appointee, Roland Burris (apparently a blameless candidate), has become Illinois’s new junior senator. As his impeachment trial began in the state Senate on January 26th, Mr Blagojevich appealed to talk-show hosts, describing his innocence and jogging habits, and boasting that he had considered appointing Oprah Winfrey to the Senate seat.

Meanwhile, the governors of Colorado and Delaware have filled the vacancies left by Ken Salazar and Joe Biden with no drama. Mr Biden’s seat, though, was filled by someone widely assumed to be keeping the seat warm for Mr Biden’s son, currently serving in Iraq.

Many would argue that gubernatorial appointments give too much power to one person and too little to voters. Since 1913 more than 180 senators have been appointed by governors, according to Fair Vote, a voting-rights advocacy group. Only four states—Massachusetts, Oklahoma, Oregon and Wisconsin—fill vacancies purely by special election.

David Segal of Fair Vote says there is no reason why a speedy election could not be held when Senate vacancies occur. Russ Feingold, a Wisconsin senator, is trying to amend the constitution to require just

that. House vacancies, after all, are filled in that manner. No fewer than 26 candidates are now vying for voters' attention in the race for the seat vacated by Rahm Emanuel when he became White House chief of staff. Recent events show that the Senate needs to bury this relic of the past.

Energy policy

Pumped up

Jan 29th 2009 | STANLEY
From The Economist print edition

North Dakota is one of many states waiting for an energy policy from Washington

“THE state of our state is strong,” declared North Dakota’s governor this month. It is a rarity. Forty-one states face budget gaps; North Dakota has a surplus of $1.2 billion. Part of its success lies in the countryside. In the summer the sun lingers over fields of wheat and sunflowers. Now darkness comes early and snow often. But there are constants in the landscape: smoking coal plants, flares from oil wells and, increasingly, towering windmills.

North Dakota is enjoying an energy boom. True, it is no Texas; it produced just 3.8% of America’s crude oil in August 2008, the most recent month for which data are available, and ranks first in wind potential but 11th in wind production. With ample natural resources, however, North Dakota produces more than twice as much energy as its 641,000 residents can consume. Now it is trying to find its place in a changing energy industry. And, like states from Oklahoma to Hawaii, it is waiting for new rules from Washington.

In some ways, North Dakota is an old-fashioned energy producer. Long drag-lines scrape the state’s surface, revealing lignite, or brown coal; 91% of North Dakota’s electricity comes from coal-fired plants. Oil also looms large. The advent of horizontal drilling—a rig drills down about two miles (3.2km), then curves sideways—has allowed companies to tap the Bakken formation in the Williston basin (see map). In November North Dakota produced an average of 212,000 barrels each day; five years earlier it produced 79,000 barrels a day. At the heart of the action is Stanley, a small town whose drugstore has a vending machine for live bait (12 leeches for $4) and whose county has lured Whiting Oil, Hess and EOG (formerly Enron Oil and Gas, EOG left the main firm before it went belly up). The boom has helped fill state coffers. Revenues from the oil and gas industry comprise about half the projected surplus for 2009-11.



But John Hoeven, North Dakota’s governor, promotes the state’s green resources too, such as crops for biofuel and strong winds. In 2000 North Dakota produced one-half of a megawatt of wind energy. Now the state has 850 megawatts in place or being built, with more than 4,000 megawatts planned (America currently uses about 25,000 megawatts of wind energy). The Energy and Environmental Resource Centre (EERC) at the University of North Dakota is a hotbed of activity, searching for ways to advance everything from zero-emissions coal plants (still nonexistent) to cellulosic ethanol.

Mr Hoeven insists that coal and oil can complement green development. In 2007 he created the Empower ND commission, a group of businessmen representing old and new energy sources, to nurture co-operation and suggest policies. Shane Goettle, the commission’s chairman, points to a project to capture a coal plant’s carbon emissions and inject them into local wells, to help recover oil. Coal plants themselves, he says, can provide backup for fickle wind turbines.

Still, uncertainty looms because of volatile prices and regulatory limbo. The price of North Dakotan crude has fallen from a high of $136 in July to $33 now. The number of rigs is dropping accordingly, from 96 in November to 71 now, and is expected to sink further. Wind-power projects are undermined by transmission problems. Gerald Groenewald, the EERC’s director, uses hay-man’s terms: “We produce the crop but we can’t get it to the grain elevator.” American Electric Power is mulling one which would transmit wind power from North Dakota to Chicago, but progress will be slow without federal help.

Perhaps most important, the row over capping carbon emissions drags on, though support from Barack

Obama’s White House will probably force the issue this year. “Coal is going to be a part of our future,” insists Byron Dorgan, North Dakota’s junior senator. Mr Dorgan wants to impose restrictions gradually, to give researchers the time and money to develop new technologies. Carbon capture and sequestration is still at a very early stage.

Without clear regulations, a plan has stalled for a $4 billion coal-to-liquid project in North Dakota. “There’s something coming,” says David Straley of North American Coal, a partner in the project, “but they won’t put their finger on what it is.” Out in the fields the oil pumps move up and down, like metronomes keeping time.

The aftermath of Hurricane Ike

Blown in the wind

Jan 29th 2009 | GALVESTON
From The Economist print edition

Texas's Gulf coast faces a long road to recovery

JAMES CLARK was not exactly surprised when Hurricane Ike swept across Galveston Island, destroying his camper and damaging his scrap of beach-front property. It was not the first hurricane to hit the Gulf coast of Texas, and not the first to hit him. "I lost my property in Carla in '61, in '83—what was that, Alicia?—and then again this time. But I'm 70, so I guess I probably won't ever learn," he said.

Mr Clark kicked the carpeted floor of the island's stately convention centre. It was January 7th, and he had turned up for a public hearing on the region's recovery from Ike. Behind him, a wall of windows showed a thin strip of beach. Half a dozen dump trucks were beetling around with loads of supplemental sand. Nearby there were piles of debris and the skeletons of houses shredded by the storm.

Ike made landfall in Texas more than four months ago. Yet Galveston and the surrounding coastal towns are far from recovery. The main issue is money. On January 12th the Federal Emergency Management Agency (FEMA) released a report estimating that the damage to Texan homes, schools, roads and general infrastructure would reach tens of billions of dollars. Private insurance will cover some of that, but many homeowners are finding that they were covered only against damage by wind, not water. In any case, the state does not have the money to fix everything at once. On January 12th its comptroller warned legislators to expect a $9.1 billion revenue shortfall in 2010-11. Texas is waiting for federal aid. And that is slow in coming—though the Galveston County Recovery Fund reports receiving a personal cheque from Barack Obama.

In the meantime, Galveston's problems are multiplying. At the public hearing, legislators spent hours listening to tales of woe from all directions. One city official said that it was uncertain how many Galvestonians had returned to the island. Before the storm the city had 58,000 residents; based on water usage, perhaps 40% are still gone. This squares with a report from the school superintendent. Enrolment is down sharply and four schools are still closed. The city manager said that despite a hiring freeze and pay cuts, Galveston is almost desperate for money. The next step will be slashing services.

Perhaps the biggest question-mark is over the future of the University of Texas Medical Branch (UTMB), a hospital complex that includes a top-ranking trauma centre and medical school. Before the storm it was Galveston's biggest employer, with 12,500 workers. But UTMB sustained more than $1 billion-worth of damage and losses, with only $100m of it insured. With most of its operations halted since September, the hospital has been losing tens of millions of dollars each month.

On the day of the hearing the emergency room was empty, tarpaulins hung in some hallways and a small white boat was marooned in an adjoining parking lot. The hospital is known for serving uninsured and underinsured people, but Brian Zachariah, the director of emergency medicine, reckons that it will have to cut back on this. In another cost-cutting measure, 2,400 workers were laid off in November.

Some Galvestonians believe that the university's regents are not doing enough to help UTMB. For if the hospital falters, say islanders, it would be devastating for the local economy—a sort of second Ike, for people still struggling after the first.

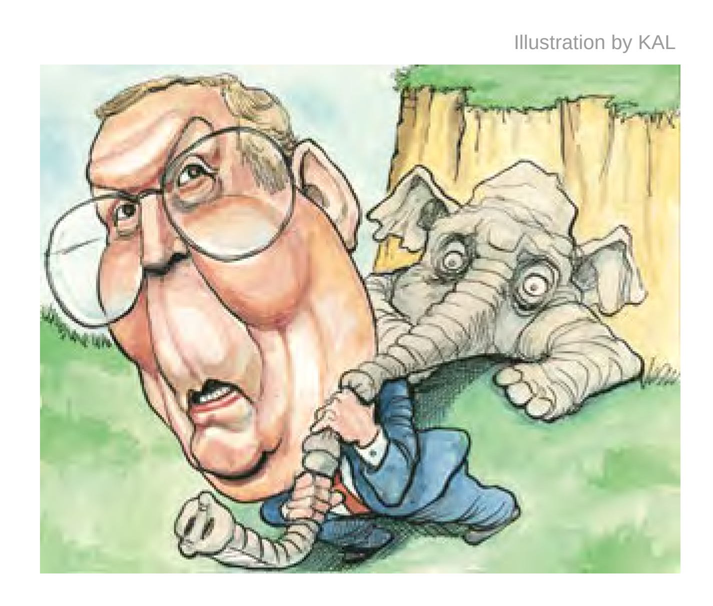
Lexington

Republicans seeking relevance

Jan 29th 2009
From The Economist print edition

Can a wrecked party with a toxic brand make a difference? Mitch McConnell thinks so

Illustration by KAL



GEORGE BUSH passed on two batons last week. Barack Obama succeeded him as the most powerful man in the world. Mitch McConnell succeeded him as the most powerful man in the Republican Party. The former handover generated, reportedly, 35,000 news stories in a single day. The latter, not so many. Not only is Mr McConnell, the Senate minority leader, far less important than Mr Obama. He is also far less comfortable in the spotlight. Scan a photo of the inauguration and you can just make him out, standing a few rows back from the new president. He looks grey, owlish, bespectacled and glum. If the Republicans are looking for a jolt of inspiration and a fresh face to lead them into battle, Mr McConnell is not their man. But it would be a mistake to underestimate him.

As a child, he overcame polio. In his early 40s, after a series of low-profile political jobs, he ran for the Senate from his home state of Kentucky. The incumbent Democrat, Dee Huddleston, looked tough to dislodge. But Mr McConnell ran wickedly entertaining campaign ads showing bloodhounds sniffing around Washington for his opponent, who had missed votes to give paid speeches in balmy resorts. The ads also showed the hounds chasing Mr Huddleston up a tree as he tried to run away from his record. Mr McConnell ousted him by a handful of votes.

“My original ambition as a senator was to someday be known for something other than the bloodhound commercial,” said Mr McConnell recently, after being introduced with yet another retelling of the story. But unlike most of his colleagues in the Senate, Mr McConnell has never shown a glimmer of presidential ambition. He is happiest stitching together deals in the dark—and he is good at it. When he ran for the Republican leadership in the Senate in 2006 he campaigned entirely behind the scenes, quietly collecting pledges of support and scaring off potential rivals by discreetly showing them that they had no chance.

Since then, Mr McConnell has strewn the Democrats’ path with barbed wire. Under Senate rules, a minority of 41 or more (out of 100 senators) can block nearly anything. Last year, with 49 seats, Republicans slowed the lawmaking process to a shuffle. This year, with only 41 seats (and one race, in Minnesota, still not settled), Republicans can thwart Mr Obama’s agenda only if they remain perfectly united. That is always hard. So Mr McConnell talks of using a mixture of co-operation and filibuster threats to influence the way new bills are drafted. This makes a welcome contrast to Republicans in the House of Representatives who have no power to filibuster and therefore little influence. The big fuss they made this week about funding for family planning smacked of point-scoring. Mr Obama sounded like a grown-up when he conceded their point and moved on.

Mr McConnell says he welcomes Mr Obama's promise of "post-partisanship". But he is not offering to surrender. He makes no secret of his unyielding hostility to some Democratic bills, such as the oddly-named Employee Free Choice Act, which would curb the right to a secret ballot before a workplace is unionised. Mr McConnell says this would "turn America into Europe", and predicts a big political fight over it.

Yet Mr McConnell's call for bipartisanship is not a total sham. He has worked with Democrats before, not least to cobble together a bail-out of the financial sector last year. He is right that Congress will probably do a better job of tackling the economic crisis if Democrats and Republicans co-operate. He is right, too, if somewhat hypocritical, when he argues that taxpayers need a watchdog to stop interest groups from treating the stimulus bill like a second Christmas. "Everybody's making their list and checking it twice," he tuts—though he has a long record of gift-wrapping taxpayers' cash for interest groups in his home state.

Some of his ideas are constructive. He wants a big chunk of the stimulus to come in the form of tax cuts. He wants to make federal cash for the states a loan, not a gift, so there is less chance it will be wasted. And when the immediate crisis is over, he wants both parties to sit down and work out how to curb the terrifying growth of entitlement spending (public pensions and health care). This makes sense. Since any plausible solution will hurt, neither party will take sole responsibility. Mr McConnell promises that Democrats "can expect more co-operation from Republicans than the last president received from them."

A new face for the Grand Old Party?

A show of reasonableness might help Republicans repair their shredded reputation. But the task is immense. The party has been walloped in the past two elections. It has negligible support among young people and ethnic minorities. And its previously cutting-edge get-out-the-vote machine looks rusty and antiquated next to Mr Obama's. The task of rectifying all this will fall heavily on the new chairman of the Republican National Committee, who will be chosen this week.

The winner must be "ever-present" on television, says Jim Nicholson, who did the job in the late 1990s. The RNC chair has two main tasks besides raising money: to fire up the base and woo new voters; and the two are in tension. All six candidates say Ronald Reagan was their favourite Republican president. That thrills conservatives, but swing voters may wonder why Abraham Lincoln gets no mention. Encouragingly, two of the leading contenders are black. But one of them, Ken Blackwell, a failed gubernatorial candidate from Ohio, shows little interest in swing voters and tends to bang on about gays. The other, Michael Steele, a former lieutenant-governor of Maryland, has broader appeal. Handsome, moderate, the grandson of a sharecropper and the only candidate who doesn't own a gun, he looks good on television even to non-Republicans. His moderation may count against him with the party faithful. But if the Republicans want to be relevant again, they need a more inclusive faith.

Canada's budget

Joining the stimulating party

Jan 29th 2009 | OTTAWA
From The Economist print edition

A pragmatic budget has given Stephen Harper's government a new lease of life—but not necessarily a long one

Illustration by David Simonds



MORE than in many countries, in Canada the question of how to respond to the world recession has become muddied by party politics. During the campaign for last autumn's general election, Stephen Harper, the Conservative prime minister, ridiculed the opposition for daring to suggest that his government might post a budget deficit in a country that has come to prize fiscal virtue. Having won a second term, though once again without a parliamentary majority, Mr Harper promptly almost lost it over a government economic statement in late November. In this his finance minister, Jim Flaherty, again rejected the need for fiscal stimulus but threw in some partisan measures. That prompted the disparate opposition to gang up to try to oust Mr Harper—a fate he evaded only by persuading the governor-general, who acts as Canada's head of state, to shut down parliament for seven weeks.

In that period the economy has slithered towards recession. So this week's budget was of more than usual interest. In the event, Mr Flaherty showed a surer touch than in November. Jettisoning his party's ideological commitment to small government, he came up with new spending and tax breaks worth C$40 billion ($33 billion) over the next two years. Much of the money will go on maintaining roads, railways and ports and in encouraging home improvements. The government is also adding C$50 billion to its C$75 billion fund to buy mortgage-backed securities from banks, to encourage them to lend. For the first time since 1996 the federal budget will move into deficit, with a shortfall of C$34 billion in the fiscal year starting in April. Deficits will total some C$85 billion before the federal finances return to the black in four years time, Mr Flaherty forecasts.

Previous Liberal governments worked hard to cure Canada of an addiction to deficit financing. In losing his fiscal virginity, Mr Flaherty blamed "the synchronised global recession". Certainly Canada is vulnerable: it has been hurt by recession in the United States, which buys three-quarters of its exports, and by falls in the prices of its commodities. Private-sector economists consulted by the government expect the economy to contract by 0.8% this year, bouncing back to growth of 2.4% in 2010. The darkening economic outlook, especially in Ontario where the car industry is concentrated, has softened public opposition to deficits.

But has Mr Flaherty got the dose right? The economy remains relatively strong. Canada’s banks are much better regulated, and sounder, than their American counterparts. The central bank began to inject liquidity into the banking system a year ago, and has slashed its benchmark interest rate to just 1%. A weaker currency (see chart) will help exporters. Mark Carney, the central bank’s governor, expects the economy to start to recover late this year (though he says this may not be apparent until early 2010). If so, monetary policy may deserve more of the credit than fiscal stimulus.

The government’s more immediate concern is survival. On this it may have little to fear for now. The separatist Bloc Québécois and the leftist New Democrats (with 86 seats between them) both said they would vote against the budget. But Michael Ignatieff, the new leader of the Liberals, whose 77 of the 308 seats in the House of Commons are vital, said he would back the budget, provided Mr Flaherty offers quarterly reports on how the extra money is being spent. “We’re putting the government on probation,” he said.



Mr Ignatieff is unenthusiastic about his predecessor’s idea of an opposition coalition. It suits the Liberals better to let the Conservatives take the blame for the recession while rebuilding their own finances, organisation and ideas. As for Mr Harper, while the budget shows that he is a pragmatist, it is not popular with some in his own party. Since November, his authority is no longer unassailable. He is living on borrowed time as well as money.

The Caribbean economies

Lonely beaches

Jan 29th 2009 | PORT OF SPAIN
From The Economist print edition

A fall in tourism, and other body blows


Rex Features

IT IS the time of year when the island nations of the Caribbean normally expect their hotels and beaches to be packed with sun-seekers. But this year, cash-strapped North Americans and Europeans are staying at home. Visitor numbers will fall by up to a third, reckons Harold Lovell, who chairs the Caribbean Tourism Organisation. The hotel association in Tobago says that only one bed in three is occupied. Atlantis, a mega-resort in the Bahamas, laid off 800 staff in November, while flights to Nassau, the capital, have been cut by a quarter. The picture is similar in the Dominican Republic, while a strong increase in tourist arrivals in Cuba tailed off in the last three months of last year.

The scarcity of tourists has halted some ambitious expansion plans, and is a blow to fragile economies. The Bahamas had approved investments worth over $20 billion over the next five years. Mayaguana, a sparsely populated island of crystal seas and white sand, was set for a $1.8 billion resort with the world's longest airport runway. Now its torpor may remain undisturbed. Baha Mar, a $2.6 billion project in Nassau that would have employed 4,400 building workers, has been stopped by the withdrawal of its American casino partner. Other large developments are on hold in Jamaica, St Lucia and Anguilla.

Since the 1990s, most big Caribbean tourism projects have been planned around second (or third) homes for babyboomers. Grand designs show a sprawl of houses and apartments arrayed around a small but pricey hotel, a golf course and marina, and perhaps a casino. Most of the development is financed by sales of unbuilt real estate, much of it as timeshares. Plunging housing markets and the credit crunch have put paid to all that.

There are other sources of woe. Trinidad's ten-year energy boom has suffered a jolt from falling oil and gas prices. Smaller islands which prospered from offshore finance worry about tighter international controls. And remittances from workers abroad have fallen.

In Jamaica, remittances shrank by an average of 14% in November and December compared with the same months in 2007. The price of bauxite, Jamaica's other big earner, has more than halved since its peak last July. Many among the island's middle class lost their savings last year (and some their homes), in unregulated investment scams.

With government revenue already below target, Jamaica has nevertheless cut taxes. Others would like to do so. But many Caribbean nations are highly indebted. With finance tight, raising cash from asset sales is harder: Jamaica failed to meet its target of privatising its sugar industry, and the Bahamas its telecoms, by the end of the year. After a decade of borrowing in the markets, Caribbean governments have once again become clients of the international development banks.



Mining in Peru

If a city's the pits

Jan 29th 2009 | CERRO DE PASCO
From The Economist print edition

Then move the city



MORE than 4,300 metres (14,000 feet) above sea level in Peru's central Andes, the cold, windswept Bombón Plateau is not an obvious place to build a new town. But plans are afoot to rehouse 70,000 people there over the next 10 to 15 years. The reason: the town of Cerro de Pasco, some 35kms (22 miles) away, is being eaten up by opencast mining.

Last month local residents voted in an assembly in favour of the plan. It is supported by Peru's president, Alan García. The country's Congress has called for detailed studies of a site around the villages of Ninacaca and Shelby.

The plan is logical. Cerro de Pasco has been mined, mainly for silver, lead and zinc, since the 17th century. Opencast mining by an American company began in 1956, and continued after it was nationalised in 1973. The city now teeters around a huge pit, two kilometres across and 350 metres deep. “There really is no city. What we have is a network of streets that end at a cement wall and a pit,” says Félix Rivera, the governor of the Pasco region, who favours the move.

Privatised again in 1999, the mine is now owned by Volcan, a Peruvian company. Its expansion plan would eat up 11 hectares of the city, pushing the wall closer to the main square. Cerro de Pasco has never been a beauty spot. But the few local landmarks, such as the main church, would disappear into the hole by 2014. Mr Rivera says that daily blasting at the pit has weakened urban areas, and that many homes are unsafe. Studies have found that residents have high levels of lead in their bloodstream.

The regional government estimates the move will cost $500m. The mayor reckons the figure will be double that. Mr Rivera recalls a past plan to uproot Cerro de Pasco, in the late 1980s during Mr García's first term as president. His government spent $30m putting in electricity posts and building small houses at a spot on a highway out of the town. But the project was abandoned.

Local politicians say Volcan should stump up half the cost of the move. The company has said little. A spokesman recognised that any position it takes would be “controversial”. If it backs the move, critics of mining among Peru's NGOs and environmentalists will accuse it of literally wanting to dig the ground from under the townspeople's feet. It it opposes the plan, it will be branded as wanting to expose people to further health risks.

In neighbouring Junín, a Chinese company, Chinalco, is proceeding with a plan to move Morococha, a town of 5,000 people, to develop a big copper deposit. This whole project will cost over $2.5 billion. Cerro de Pasco is a much bigger place. In the past few months the prices of minerals have plunged. Work on Volcan's expansion plan has slowed. So Cerro de Pasco's big move is far from certain.

Japan's politics

The Fat Lady is about to join in

Jan 29th 2009 | TOKYO
From The Economist print edition

Even its own members reckon Japan's ruling LDP faces annihilation

AFP



THE wave which first broke in earnest over Japan's economy towards the end of last year now looks set to sweep away a political system dominated for half a century of almost unbroken power by the Liberal Democratic Party (LDP). That, at least, is now the view of parliamentarians of all stripes. This week, a poll by the *Nikkei* newspaper saw the government's approval rating fall to 19%, abjectly low. Morbid LDP members admit that a party that has seen four prime ministers in as many years is not just bereft of ideas but has lost the stomach for a fight. The government, they say, will plop into the lap of the opposition Democratic Party of Japan (DPJ) in an election that the prime minister, Taro Aso (pictured above), has to call by September.

Mr Aso deserves a scintilla of credit for trying. Though he assembled a cabinet of exceptional mediocrity last September, he expected to call a snap election while his approval ratings were still fairly high. Mr Aso was then faster than most to grasp the severity of the global slowdown, and that Japan, its economy driven by exports, would be disproportionately hit. More than once he has put off calling an election in order to confront the slowdown. He saw through stimulus measures and loan guarantees inherited from his predecessor. He announced a second stimulus, including a ¥2 trillion ($22 billion) cash handout to households. And he declared that nothing so frivolous as an election would disrupt preparations for the full budget for the fiscal year that begins in April, in which the economy would get another boost. This was to be Mr Aso's three-stage rocket.

It has turned out to be a damp squib. The new spending is not large, yet promoting the proposals has consumed his political capital. For a start, instead of pushing the second stimulus through the Diet (parliament) at once, Mr Aso put it off until the session that began in January, so as not to divert energies from the annual budgeting ritual. Yet that has given more time for the public to turn against the handout as a gimmick, and for the opposition to make hay. Citing the handout, one prominent LDP member, Yoshimi Watanabe, a former financial-services minister who has long been unhappy about the lack of administrative and supply-side reforms, stomped out of the party on January 13th.

Mr Watanabe's departure set off speculation about whether civil war within the LDP was about to break out into the open, with defections to a new political force. If only in this respect, the scale of Japan's slump benefits Mr Aso for now, since it has stilled such a rebellion. The most powerful critic of the LDP's lack of reform zeal, Hidenao Nakagawa, a former party secretary-general, now says that political

realignment must happen only when voters demand a clearer direction. He will not, he says, be the one to fire the assassin's shot at Sarajevo. And Yasuhisa Shiozaki, a former chief cabinet secretary, has not accepted Mr Watanabe's entreaties to join him. Rather, Mr Shiozaki says, he and a few colleagues will push for a new stimulus package worth ¥10 trillion—this time tied to changes in highly regulated areas such as health care, education and agriculture.

Potential rebels share two other calculations. Mr Aso might yet bow out, allowing one more boundlessly self-regarding buggins to contest the next election for the LDP. The second is that as the chances rise of an outright victory by the DPJ in the next election, so the leverage of any third political force diminishes. A wholesale political realignment in Japan may have to wait until the DPJ attains office and stumbles.

In the meantime, says Tadamori Oshima, the LDP's Diet-affairs chief in the lower house, the odds of Mr Aso's passing his various packages have shortened. On January 27th the second stimulus package was bulldozed through. Until recently, a move led by Mr Nakagawa and Mr Shiozaki looked as if it might derail passage of the next fiscal year's budget. To pass enabling legislation, the ruling coalition must use its "supermajority" in the lower house to override the opposition-controlled upper house. But the rebels had objected to language about the need to raise the consumption (sales) tax in 2011 in order to finance social welfare. The rebels backed down after it was made more explicit that the rise hinged not just on economic recovery, but on reducing the power of the bureaucracy. Mr Oshima now says he is certain that the supermajority, without which Mr Aso would have to resign, will hold.

This brings only a brief respite for the prime minister. The economy is worsening fast: in December year-on-year exports fell by 35%; surveys of consumer confidence are at all-time lows; while the central bank talks of an economic "emergency". This week, the government announced convoluted plans for public funds to be used to buy shares in cash-strapped smaller companies. Though it has not been announced, it also wants to force big city banks to take public-capital injections, with no strings attached, rather than risk sending the stockmarket down further by issuing fresh shares. If Mr Aso plans further stimulus packages, publicising them now might only heighten the tooth-pulling pain of passing the current measures.

In his policy speech to the Diet on January 28th, the prime minister promised to bring Japan out of recession before the rest of the world, yet he gave few clues as to how. Admittedly, he expounded on the need for sweeping changes to the tax system, including raising the consumption tax. By mentioning the tax, Mr Aso meant to signal his commitment to responsible politics. Yet nothing he said hinted at tough structural changes to promote growth. Drained of influence and written off by his own party, a single weapon remains with Mr Aso: when to dissolve the Diet and call the election. As to when he will do that, says Mr Oshima, probably the prime minister's closest and most important ally, only Mr Aso and God know.



WORLD
ASIA

Cambodia's disappearing capital

Lake inferior

Jan 29th 2009 | PHNOM PENH
From The Economist print edition

The poor pay for a property boom

Reuters



Be it ever so humble

THE fading colonial charm of the French-built Renakse Hotel in Phnom Penh has faded for good. The last guests have been pushed out and the windows boarded up. A property boom in the Cambodian capital has brought a whirl of demolition of old buildings, plans for new high-rise developments, and speculative investment in satellite towns.

The victims of this have been Phnom Penh's poor. Last week police and private security guards roughly evicted 120 families from Dey Krahorm, a slum in the centre of the city, on the orders of Phnom Penh's governor. The firm developing the area, 7NG, is linked to the ruling Cambodian People's Party, the CPP, led by Hun Sen, the prime minister. The company plans to turn the site into an upmarket retail park. Nearby, a famous park area known as the Boeung Kak lake is also to be developed, bringing the eviction of 4,500 residents. Many had been living around the lake for 20 years. They have been offered only paltry compensation, and have been relocated to the city's outskirts with no amenities or obvious way of making a living.

The controversial plans involve filling in 90% of the lake. The CPP has ditched past commitments to conservation and environmental protection, as the boom has driven prime-land prices in Phnom Penh up tenfold in two years, to $5,000 per square metre. The municipal government has granted a 99-year lease on 133 hectares (330 acres) of the Boeung Kak site to a CPP senator, Lao Meng Khin, who is also a director of a company called Shukaku, for a mere $79m—a fraction of its estimated true market value. In April 2008 Mr Khin signed a deal with a Chinese company to turn the lake area into a posh residential and recreation development, to be dubbed the "New City of the East". A Korean company is building a similar city, known as CamKo, on Phnom Penh's outskirts.

Critics say the Boeung Kak deal is illegal. Cambodia's 2001 land law declares all lakes public property that cannot be leased for more than 15 years. The authorities say the deal was legalised by a 2008 decree from Mr Hun Sen's cabinet, reclassifying "state-public land" as "state-private land".

Mok Mareth, the environment minister, initially raised concerns that filling in the lake would do serious damage to Phnom Penh's drainage system. This, he argued, would violate a 1996 law ordaining that Cambodia's natural resources should be conserved, developed, managed and used in a rational and sustainable manner.

Indeed, since August 2008 when developers started filling the lake in, some houses have already started sinking. An independent report released earlier this month by an Australian assessment team gave a strong warning against the project. It concluded it would lead to an increase in flooding, and would endanger water quality and public health.

Two decades ago, children paddled boats on the lake, families enjoyed picnics, and Mr Hun Sen used to entertain foreign visitors at a modest but picturesque bamboo restaurant. But today, as the bulldozers are poised to raze old Phnom Penh and plug its favourite lake, the urban poor are starting to feel nostalgic for a time when a park really was a park and not a so-called “state-private development zone”.



Fiji and the Pacific Islands Summit

Doing it his way

Jan 29th 2009 | CANBERRA
From The Economist print edition

The neighbours worry about Fiji



GATHERING in Port Moresby, capital of Papua New Guinea, Pacific Island leaders this week gave an absent friend an ultimatum. They told Fiji's coup leader, Frank Bainimarama, that if he fails to announce credible plans for an election this year, Fiji will face suspension from the Pacific Islands Forum. If Mr Bainimarama's international standing is on the line, so is the Forum's own credibility.

Mr Bainimarama, who took office as interim prime minister after a coup in December 2006, stayed away from the meeting in Port Moresby, a Forum summit. He pleaded pressing domestic duties after severe floods in Fiji in early January. Few in Fiji believe that excuse. More likely, he was embarrassed to face the Forum after breaking a firm promise to hold elections by March 2009. This is not the first time Fiji's coup leader has snubbed a regional summit: last August he failed to attend a similar meeting in Niue, one of the microstate members of the Forum. Confirming the impression of disarray in Fiji diplomatic circles, the most senior official in the foreign ministry was forced to resign this month after saying on local television that he wished Mr Bainimarama would indeed attend the Port Moresby meeting.

Mr Bainimarama insists that sweeping electoral reforms have to be enacted before the next polls. These, he says, could then be held 12-15 months later. He claims that Fiji's voting laws have fuelled racism and underpinned the country's "coup culture", which has seen elected governments toppled in 1987, 2000 and 2006. His government wants to ditch Fiji's highly complex voting system, lower the voting age from 21 to 18 and abolish race-based electoral rolls, under which the country's 57% indigenous population vote separately from the 38% Fiji Indians. All these proposals may be sensible enough. But Mr Bainimarama has no mandate to enact any of them. To solve that conundrum, he hopes that the Commonwealth and the United Nations will help him arrange a "President's Forum" aimed at persuading Fiji's political parties to sign up to his reform package. But New Zealand's prime minister, John Key, has rejected UN and Commonwealth intervention, saying that the Forum is the right body to deal with Fiji.

In Port Moresby both Mr Key and Australia's prime minister, Kevin Rudd, pressed for a tough response on Fiji. Other Pacific leaders, including the host, Papua New Guinea's prime minister, Sir Michael Somare, urged a milder approach, more in tune with what they like to call the "Pacific way". After the final communiqué, Mr Rudd said that there was unanimity, and that Fiji will be automatically suspended from the Forum if no road-map towards an election is agreed by May 1st. Not everyone shares Mr Rudd's confidence.

Mr Bainimarama's initial, unscripted reaction was belligerent, likening the ultimatum to a declaration of war. With luck, wiser counsel will prevail. If the communiqué strengthens the position of moderates in his interim cabinet, and produces a firm electoral timetable, it will have achieved a useful purpose. But if Mr Bainimarama and his shadowy Military Council continue to reject any plans for a return to democracy, the Pacific Islands Forum will be forced to act later this year, or risk losing whatever credibility it still enjoys.

Sri Lanka's war

Where have all the people gone?

Jan 29th 2009 | KILINOCHCHI
From The Economist print edition

The army shows off its victories; questions mount about the cost



ONCE so teeming that Tamil Tiger rebels deployed “traffic police” at its junctions, Kilinochchi is today a desolate, shell-shocked town of headless buildings and crumbling walls. During a tightly controlled tour on January 24th, the army escorted journalists through vast swathes of northern territory—including Pooneryn, Paranthan and Elephant Pass—recently wrested from the Liberation Tigers of Tamil Eelam. Further east, fighting is in one of the bloodiest phases in the 25 years of conflict. The press must rely on officially guided visits to glean first-hand information. The fate of a quarter of a million civilians trapped in a Tiger-controlled pocket of territory remains precarious and unknown.

The Tigers had nurtured Kilinochchi into a showpiece capital, to convince foreign governments that they were capable of providing effective administration for the homeland they hoped to carve out for Sri Lanka’s Tamil minority. Their own police force and judiciary had their headquarters here. And inside the plush meeting room of their peace secretariat, international envoys would sip tea with S. P. Thamilselvan, the Tigers’ political chief, and discuss how to end decades of hatred and mistrust. Soldiers now point out a nearby patch of ravaged earth, where Thamilselvan was sleeping in November 2007 when an air force plane dropped the bomb that killed him instantly.

Kilinochchi is a sorry mess of shrapnel-riddled homes, shops and other scorched, roofless structures. Wildflowers grow among the grasses and butterflies flutter against the boom of distant artillery fire. Nature flourishes in the absence of human life. An Indian journalist was heard asking an army officer where the people were. Gone, came the answer. Thousands of families converged on Kilinochchi when battles broke out elsewhere in the Wanni. But by the time the army moved into the town in January, they had been displaced into the district around Mullaitivu.

They are now trapped in a small and shrinking patch of jungle as the war grinds on to its bitter end. Brigadier Udaya Nanayakkara, the army’s spokesman, says the Tigers are confined to 300 square km (116 square miles). The government accuses the rebels of holding the estimated 250,000 civilians with them as human shields. The army has designated a “safe zone” for them inside Tiger-controlled territory, and has promised not to fire at it.

But the United Nations and the International Committee of the Red Cross (ICRC), who have staff in the area, maintain that civilians are dying or being wounded as artillery shells explode around them. They do not say who is responsible but are urging the warring factions to let civilians leave the combat zone. In a statement from Geneva, the ICRC’s Jacques de Maio said hundreds have been killed, and the scores of wounded are swamping understaffed, ill-equipped medical facilities. He said hospitals and ambulances had been hit by shelling and several aid workers injured while evacuating the wounded. The terrified population is in need of protection, medical care and basic assistance. It has nowhere safe to seek shelter and is unable to flee. Mr de Maio called for decisive action to stop further bloodshed. Time, he said, is running out.

The government and the Tigers are trading allegations. The pro-rebel TamilNet website accused the army of keeping up a “continuous inhuman artillery barrage” on the safe zone. Brigadier Nanayakkara denied any firing into the safe zone. He also said the Tigers have told their cadres to fight in civilian clothes, and that “the moment they get killed, they go into the civilian category”.

Politics in Bangladesh

Back to normal

Jan 29th 2009 | DELHI
From The Economist print edition

An inauspicious rebirth for parliamentary democracy

PARLIAMENT in Dhaka was this week restored to its intended use; parliamentarians, sadly, returned to their old abuses. A makeshift prison for much of the two years, ending in December 2008, that Bangladesh was ruled by an army-backed interim government, the parliament complex housed the leaders of the two big political parties: Sheikh Hasina of the Awami League (AL) and Khaleda Zia of the Bangladesh Nationalist Party (BNP).

On January 25th, however, a month after the league won a general election by a landslide, parliament reconvened for the first time. True to old form, the opposition BNP walked out in protest. The reason was bizarre: it claimed that the president, Iajuddin Ahmed—whom the BNP had picked in late 2006 as the head of a caretaker government to oversee (and rig) an election due in January 2007—had violated the constitution by failing to hold the vote on time. Three days later, it walked out again, miffed at seating arrangements.

On January 22nd the league had won another landslide victory; this time in elections in the country’s 481 *upazilas* (subdistricts). Candidates it backed won more than two-thirds of the seats. But unlike the general election, these polls were dodgy. Stuffing of ballot boxes, “capturing” of polling booths and voter intimidation were rife. Three people were killed, 150 injured. Observers blamed both parties.

Both BNP and AL governments have failed to hold local elections, preferring to grant MPs complete control over lucrative development spending in their fiefs. The interim government forced the parties to hold them in the hope of reforming the highly centralised political structure.

The new AL government presents itself as the agent of “change”. But its policies mostly rely on institutional improvements made by the interim regime: an effective Anti-Corruption Commission (ACC); an independent Election Commission and judiciary; and the reform of the country’s hugely inefficient public sector. The government is also to ratify most of the laws made by the interim government (otherwise, doubt might be cast on the validity of the election it won). But the fear is that it and the BNP will shake off the straitjacket designed to prevent their return to their past confrontational excesses.

Mercifully for the new government, the impact of the global economic downturn has so far been limited. The capital account is in effect closed, which has proved a blessing. But the economy is built on clothing exports, and remittances from the Gulf. Both will inevitably suffer. The government has vowed to reduce the number of poor people from 65m to 45m during its five-year term, tackle inflation, terrorism and a crippling power crisis, and pursue better relations with India, its huge, economically important neighbour. This month it slashed fertiliser prices by half, cut the price of diesel, and revived powers to fix the prices of essential commodities.

The government’s other ambitious project is the prosecution of those accused of war crimes during the war of independence in 1971. Many of the alleged perpetrators are still active in politics, mostly as members of the Jamaat-e-Islami, a large Islamist party that did badly in the election. The interim government did not pursue war crimes, in part because of the feared economic ramifications: Saudi Arabia, a big source of remittances, objects to trials. But Sheikh Hasina, daughter of Mujibur Rahman, the murdered independence leader, said this week that she was “pledge-bound” to bring war criminals to justice.



WORLD
ASIA

India's urban environment

Heavy baggage

Jan 29th 2009 | DELHI
From The Economist print edition

India's capital tries to ban plastic bags and much else besides

A CITY of 16m people, Delhi struggles to provide its residents with adequate water, decent sewers and steady electricity. But in a kind of urban leapfrogging, its failure to provide basic amenities has not discouraged it from pursuing modish causes. In recent months the city has revived its efforts to curb honking, smoking and the pestilence of plastic bags.

January 1st was declared "No honking day" by an NGO backed by the Delhi traffic police, which threatened to fine any driver blowing his horn without good reason. The day passed without any discernible drop in noise. The state government has shown more zeal in enforcing a national ban on smoking in public places. Its "mobile squads" have fined over 4,000 smokers (many of them on buses) since the law came into effect in October. It has also approved a plan to "decentralise enforcement", by allowing hoteliers, shopkeepers and restaurateurs to impose fines on the city's behalf.

The ban on plastic bags, introduced in January, is equally ambitious. Bags litter the roadside and decorate the city's trees with a polythene blossom. Cattle ingest them and drains are clogged with them. J. K. Dadoo, the most senior bureaucrat in Delhi's environment department, blames them for the 2005 floods that killed hundreds in Mumbai. Thinner bags are a particular menace, because they are of little value to Delhi's "rag-pickers", who sift rubbish for anything they can sell or recycle. "By touching the bag and feeling it, the rag-picker knows its value," says a scientist.

The government has tried to curb plastic bags before. But its regulations were recently found wanting by the Delhi High Court, which then banned bags in markets and shops, as well as hotels, hospitals and malls. It also banned thin bags (less than 0.04 millimetres thick) outright. This should make enforcement easier. Plastics manufacturers complained to Mr Dadoo, who could say his hands were tied by the court.

Recalcitrant baggers could, in principle, face fines of up to 100,000 rupees ($2,000) or up to five years in jail. The penalties have to be stiff, says Mr Dadoo, since "the desire to pay the penalty is sometimes greater than the desire to change your mindset." But the government plans to act against manufacturers before shopkeepers or their customers. First restrict availability, then the habit may change, they argue.

It may be an uphill struggle. In Delhi, "Civic sense leaves a little to be desired," says Mr Dadoo. It is sometimes described as "nobody's city", inhabited by refugees from India's 1947 Partition or by job-seeking migrants. One of the department's campaigns declares, "Delhi is my home. My city. And I am proud of it." Delhi's honking, smoking, littering residents perhaps need this gentle reminder.

Congo and Rwanda

An arresting and hopeful surprise

Jan 29th 2009 | GOMA
From The Economist print edition

By nabbing one of Congo's toughest warlords, Laurent Nkunda (pictured), Rwanda seeks to bring peace to the ravaged borderland between the two countries

Getty Images



THE capture of a Congolese warlord, Laurent Nkunda, surprised almost everyone, not least the preening man himself. As commander of the National Congress for the Defence of the People (known by its French initials, CNDP), he claimed to be protecting fellow Tutsis in eastern Congo from Hutu *génocidaires* of the Democratic Forces for the Liberation of Rwanda (FDLR), and, in consequence, the interests of Rwanda's Tutsi-dominated government across the border. Despite causing mayhem in eastern Congo last year, Mr Nkunda plainly had the backing of Rwanda's president, Paul Kagame. Not any more.

The austere Mr Kagame was increasingly embarrassed by reports, particularly a recent one by a panel of experts under the aegis of the United Nations, who detailed extensive links between Rwanda and the belligerent Mr Nkunda. The revelations were undermining Mr Kagame's efforts to attract foreign investment to transform his tiny country into "Africa's Switzerland". Britain, Rwanda's most generous backer, gave warning that it would cut its aid if Mr Kagame did not clean up Rwanda's act in next-door Congo.

The poor condition of the Congolese army and the inability of Congo's president, Joseph Kabila, to project power into his country's east gave Mr Kagame the opportunity to strike against his erstwhile ally. The two heads of state agreed to a simple swap. Rwanda would break up the CNDP and hand over Mr Nkunda, with a proviso that the CNDP's fighters would be integrated into the Congolese army. In return, Congo would let several thousand Rwandan troops cross the border and smash up the Hutus' FDLR. The UN's large peacekeeping force in the area, which both countries had lost confidence in, would be told nothing of the operation in advance.

Mr Nkunda slipped into Rwanda last week still believing that his furtive friendship with Mr Kagame would protect him. He was probably on his way to a secret meeting with senior Rwandan officials. But now the so-called "butcher of Kisangani" (a reference to the atrocities committed by his militiamen in that Congolese town several years ago) is under house arrest in Rwanda. He may give away many Rwandan state secrets if he is handed over to the Congolese authorities, who want to try him for war crimes. But Mr Kagame must reckon he has more to gain by removing him than by propping him up. His advisers say they hope for a rapid improvement in security in and around the Congolese town of Goma, near

Rwanda's border.

It is a risky strategy, for both Rwanda and Congo. By bringing the CNDP into Congo's army and reducing the Hutus' FDLR to shards in the forest, security in eastern Congo could worsen, with smaller and more erratic gangs of often drunken gunmen looking for ever nastier ways to make money and have fun. The UN fears this could lead to yet more slaughter and displacement of civilians. A lot depends on the intentions of Messrs Kabila and Kagame. Congo needs to show its resolve by disciplining its army. Rwanda has to demonstrate restraint, avoid looting and quickly withdraw the several thousand troops it now has in Congo. Neither will be easy.

Pessimists say Mr Kabila acted out of desperation. With Congo's economy in tatters, its government near-bankrupt and his popularity plummeting, the young president needs a victory. If the two neighbours do squash the FDLR and bring a semblance of peace back to the east, Mr Kabila could revive the peacemaking image that a little over two years ago helped him win Congo's first democratic elections in more than 40 years. But in the short run his decision to invite Rwandan soldiers into Congo has met stiff resistance from enemies and allies alike, who remember that Rwanda has invaded Congo twice in recent memory, both times to terrible effect.

Mr Nkunda's extradition by Rwanda to Congo could take some heat off Mr Kabila and help him sell a seemingly unholy alliance with Mr Kagame to the sceptical Congolese: a tricky task. But powerful soldiers in Rwanda's army are apparently loth to hand Mr Nkunda over.

Still, Rwanda has more to gain by co-operating with Congo. Rwanda's economy grew tidily in 2008, with revenue from tea, coffee and tourism. As a new member of the East African Community, it can earn more by openly handling Congo's metals, gems and hardwoods than it can by looting them, as in the past. If Mr Nkunda and other alleged war criminals, such as another warlord, Congo's Thomas Lubanga, whose trial has just begun at the International Criminal Court in The Hague, are sent to prison, hundreds of thousands of displaced Congolese may feel safe enough to start going home. It may even be the beginning of the end of a long, hellish period of impunity in the tragic heart of Africa.

Zimbabwe

Will power really be shared?

Jan 29th 2009 | JOHANNESBURG
From The Economist print edition

A claimed breakthrough may still not end the political impasse

A DEAL or not a deal? That is the question. On January 27th Kgalema Motlanthe, South Africa's president, who is also chairman of the Southern African Development Community (SADC), declared after an all-night meeting of the 15-nation regional club that a "unanimous" agreement had at last been reached to set up a power-sharing government in Zimbabwe by February 13th. This would end 11 months of instability, international isolation and a growing humanitarian crisis. That, at least, is the hope.

Under the deal, Morgan Tsvangirai, leader of the opposition Movement for Democratic Change (MDC), would be sworn in on February 11th as prime minister of a coalition government. The ministers, to be assigned their portfolios in accordance with a SADC agreement last November, would be sworn in two days later. Robert Mugabe, who turns 85 on February 21st, would remain as president.

But the MDC promptly denounced the arrangement. It fell "far short of our expectations", the party said, and resolved none of the outstanding issues, such as its demand for certain key ministries, including home affairs (which controls the police), and a definition of the president's and prime minister's relative powers. The composition of the powerful National Security Council was also unclear. Indeed, this new package looked very much like the one the MDC firmly rejected three months ago.

It began to look as if SADC, after its failed mediation over the past two years, may be claiming a breakthrough to save face. This appeared credible when Mr Tsvangirai's own spokesman said it was "completely malicious" to suggest that the MDC leader had signed up. But then Mr Tsvangirai himself declared he had indeed agreed to the formation of a coalition government—although the proposed timetable was not cast in stone and could be altered if problems remain unresolved.

So what is going on? A power struggle may be under way behind the scenes between Mr Tsvangirai and Tendai Biti, the MDC's general secretary and its reputed brains. Having reportedly opposed the original power-sharing deal between Messrs Mugabe and Tsvangirai in September, a harder-line faction led by Mr Biti now hopes to persuade the party to reject the latest one at a meeting of its national council. It would then refer the matter to an African Union summit in Ethiopia's capital, Addis Ababa, and later to the UN, a strategy apparently backed by the United States and Britain.

AP

Tsvangirai in a squeeze

They have long supported the MDC in the hope that it would eventually kick the ever-more-despotic Mr Mugabe out at the polls. The MDC nearly succeeded last March, when Mr Tsvangirai beat Mr Mugabe in the first round of a presidential race and the MDC won a majority in a concurrent general election, though it remained in a minority in the Senate. Mr Tsvangirai pulled out of a much-delayed run-off for the presidency after more than 100 of his people were murdered and thousands beaten up, arrested and tortured in government-sponsored violence. Both the United States and the EU, Zimbabwe's biggest donors, have said they will not resume aid until a power-sharing government is set up. The EU squeezed Mr Mugabe harder this week by adding 27 Zimbabwean officials and 36 companies to a black list, with assets frozen and travel in Europe barred.

Meanwhile, the catalogue of disasters is lengthening. A cholera epidemic has killed more than 3,000 Zimbabweans and infected nearly 60,000 others. The country's health-care system has all but collapsed. The sick and the pregnant are being turned away from hospitals for want of medicine and staff. Most schools and universities have closed. Inflation, at an estimated 2 billion per cent a month, has rendered the country's currency worthless. Furious troops have gone on the rampage, demanding to be paid in

American dollars or South African rand, the only currencies now accepted in many shops. The central bank, which recently said it would issue notes for 100 trillion Zimbabwe dollars, is reported to have drawn up plans for an informal “randisation” of the economy, with all civil service salaries to be paid in rand within six months, though how this would be financed is anyone’s guess.

In the past few months, an array of foreign leaders (though few African ones) have been calling for Mr Mugabe’s removal. Some people, such as South Africa’s Desmond Tutu, a former archbishop, have even suggested using force. Just before the latest deal was announced, America’s new secretary of state, Hillary Clinton, said she was “very concerned” about the situation. But without the concerted backing of Zimbabwe’s neighbours, there seems little that she or anyone else can do.

Diplomacy after the Gaza war

A long and bumpy road

Jan 29th 2009 | CAIRO AND JERUSALEM
From The Economist print edition

Foreigners are trying yet again to bring peace to Israel and Palestine

AS AN array of diplomats intensify their efforts to consolidate the ceasefire that took hold in the Gaza Strip after January 18th, the battered territory's 1.5m people were still gasping for desperately-needed help. Gazans are terrified that violence might return, as tit-for-tat attacks resumed at a relatively low but still dangerous level. Most Gazans now rely on food handouts to survive. Meanwhile, representatives of Israel, various Palestinian factions and the European Union, as well as America's new peace envoy, George Mitchell, converged on Egypt's capital, Cairo, to hash out the terms of a more lasting peace.

The talks covered not only the securing of a formal ceasefire and getting immediate humanitarian aid into the stricken territory, but a range of other tricky issues. These included longer-term arrangements for Gaza's border crossings, the fate of a kidnapped Israeli soldier held by Hamas and of thousands of Palestinians held by Israel, and a power-sharing deal between Hamas and its rivals. If Hamas were bound into a broader Palestinian government, outsiders could help the Palestinians while still not dealing directly with the Islamist group, which has preserved de facto control of Gaza despite the ferocity of Israel's three-week assault.

Neither Israel nor Hamas wants the fighting to resume. Both have signalled that they would accept a year-long ceasefire; Hamas has privately hinted at 18 months. Egypt suggested February 5th as a starting date. Hamas has also said it could accept international observers inside Gaza's borders to monitor the ceasefire. The Islamist party, which seized control of the territory from the Palestinian Authority (PA) run by the rival Fatah group in 2007, insists that the borders must be fully opened to trade. But Israel, which has blockaded Gaza since Hamas took over, is determined to maintain strict inspections in any circumstance. Israel is still, for instance, blocking shipments of cement and reinforced steel for building, on the ground that they may serve military purposes.

Despite the pressure for calm, Israeli aircraft came back to bomb the smuggling tunnels under the Egypt-Gaza border on the night of January 27th, putting hundreds of Gazans to flight yet again. That wave of attacks, said Israel, was in reprisal for a bomb that hit an Israeli patrol on the Gaza-Israel border, killing a soldier. Hamas, which denied responsibility for that blast, then responded by launching a rocket, which landed harmlessly in Israel.

The border bomb was probably laid by a small group, World Jihad. But Israel said it held Hamas responsible. The country's three main leaders, Ehud Olmert, Tzipi Livni and Ehud Barak, respectively prime minister, foreign minister and defence minister, all insisted publicly that drastic retaliation was needed to bolster the deterrence they claim to have re-established as a result of the Gaza campaign.

The new envoy's priorities

In any event, Israel's ministers were plainly anxious to complete that round of reprisals just before Mr Mitchell landed in Israel. He was expected first to focus on bolstering the ceasefire, channelling reconstruction aid through the Fatah-run PA rather than Hamas, and on measures to stop arms reaching Gaza via tunnels under the border with Egypt or by sea from Iran.

To this end, the Americans and Danes were planning a conference in Copenhagen in early February. France, Germany and other European governments could join a naval force, perhaps under NATO's aegis, to patrol the sea off Gaza. Egypt, nervous that foreign troops on its side of the Gaza border might undermine its sovereignty in the Sinai desert, will probably also attend the meeting in Denmark. Israelis say they are gratified by how seriously foreign governments, especially America's new one, are taking the challenge of stopping Hamas from rearming with rockets.

In a marked change of tone, Israeli officials have also praised Egypt for its stern attitude to Hamas and for its efforts to stop the smuggling, despite the bile poured on the Egyptians by Hamas's many admirers. So Israel may drop its objection to Egypt's long-standing demand to increase the size of its border force, which is limited by a mutual treaty. While Egypt has found it hard to block the tunnels, it has kept its official border with Gaza sealed to all but a trickle of humanitarian traffic, saying that the crossing's Palestinian side should be controlled by a proper government body, such as the PA, but not by Hamas.

Israel still wants to link a full reopening of the crossings to the release of its kidnapped soldier, Gilad Shalit. Hamas so far rejects such a link, insisting on a separate prisoner swap. But Israel's rulers, challenged by rivals on the right, would find it hard to give ground on this sensitive issue in the run-up to a general election on February 10th. France's president, Nicolas Sarkozy, summoned Corporal Shalit's father to Paris to reassure him that his son, a dual French-Israeli citizen, was still alive.

If the fighting has bolstered Israel's right, the Palestinian factions aligned with Hamas also think it has boosted them. So they are sure to drive a hard bargain with Fatah as efforts to create a national unity government get going. Egyptian mediators want formal Fatah-Hamas reconciliation talks to start on February 22nd, but do not expect elections that would let the Palestinian people decide who they want to run their affairs to be held before next year. Yet without a unified Palestinian front it will be hard, if not impossible, for Israel to negotiate a peace that might endure.

Israel and Turkey

Bad new vibrations

Jan 29th 2009 | ISTANBUL
From The Economist print edition

The special relationship between the Turkish and Jewish states is at risk

WIDESPREAD outrage over Israel's assault on Gaza has sharply soured the tone of Turkey's people and government towards the Jewish state. The prime minister, Recep Tayyip Erdogan, castigated it for hammering the Palestinians. So far he has resisted a clamour in Turkey to loosen or even sever his country's close ties with Israel. But some advocates of the strategic friendship between the two countries fear it may be at risk.

Behind the scenes, Turkish policymakers, especially military ones, still cherish their ties with Israel. Speaking this week in Switzerland, Mr Erdogan seemed keen to draw a line under the row. He explained that he was incensed by the war in Gaza particularly because his tireless mediation had brought Israel and Syria close to a deal over the Golan Heights. He said he had also been trying to fix a deal with Hamas over a prisoner exchange, including freedom for a kidnapped Israeli corporal.

Similar rows have occurred before. In 2004 he annoyed Israel by calling it a terrorist state after it assassinated Hamas's founder, Sheikh Ahmed Yassin, as he left a mosque in Gaza. Mr Erdogan then invited Khaled Meshaal, Hamas's present leader, to visit Turkey. But Israeli-Turkish relations were mended after prodding by the United States. Military co-operation went on. Israel has invariably chosen to turn a deaf ear to Turkey's occasionally fierce rhetoric for the sake of that strategic liaison. In a bid to soothe the anger of Jews and Israelis, Turkey's foreign minister, Ali Babacan, urged Hamas to decide "whether it wants to be an armed group or a political movement".

But this time Mr Erdogan had been a lot angrier. Israel, he railed, was "committing a crime against humanity…The world must not turn a blind eye to Israel's savagery…How can such a country, which totally ignores and does not implement the UN Security Council's resolutions be let through the gates of the UN?"

An education ministry circular particularly annoyed Israel by telling Turkish schoolchildren to observe a minute's silence in solidarity with Palestinian children. In the event, the Israelis persuaded the Turks to cancel a proposed essay and drawing contest for schoolchildren to air their feelings of hatred towards Israel. Israeli officials were apparently poised to respond by proposing a programme in Israeli schools for discussing the genocide of Armenians by Turks in the first world war.

In any case, anti-Israeli anger on Turkey's streets rose during the assault on Gaza. In rallies across the country demonstrators chanted "Killer Israel! Nazi Israel! Turkish armies, march on Jerusalem!" Calls to boycott Israeli goods and scrap military co-operation grew louder.

Not for the first time, anti-Semitism reared its head. In the western city of Eskisehir, members of a nationalist group brandished placards that read, "Only dogs can enter: no Armenians or Jews!" An outcry from Turkey's 25,000-strong Jewish community, plus pressure from the foreign ministry, shamed a local prosecutor into launching a probe. Turkey's Jewish community issued a rare statement saying that "we Turkish Jews, an inseparable part of the Turkish Republic, feel deep sorrow for the comments appearing in recent days in certain media outlets that belittle and insult our religion and present us as targets."

An ancient alliance

Turks deny accusations of anti-Semitism, noting that the Ottoman Sultans opened their doors over 500 years ago to Jews fleeing from Christian persecution in Spain. In 1948, Turkey was among the first countries to recognise Israel. Under a military co-operation deal in 1996, Israeli pilots have been training in Turkish skies. In 2007, bilateral trade rose to $2.7 billion. Between 2006 and 2007, the number of Israelis visiting Turkey went up from 362,000 to 511,400—more than 7% of Israel's population. Turkey

has also earned praise from the Americans for its recent mediation between Syria and Israel.

But anti-Semitism is often part of a general anti-Christian and anti-Western feeling. “Jew” and “Armenian” are both often used as slurs. Last year a Pew Global Attitudes Survey found that anti-Jewish sentiment in Turkey had risen: 76% said they had negative views towards Jews, whereas only 7% said they looked kindly on them.

Anti-Semitism was also blatant during a campaign against an Israeli financier, Sammy Ofer, who had planned to invest with a Turkish partner in rehabilitating Istanbul’s historic Galata district and its port near the Golden Horn. The tender was cancelled amid widespread claims that the deal was crooked and that “Jewish capital” was trying to take over the country.

Radical Turkish Islamists have long tried to stir up anti-Semitism. Their long-standing jibe against the secular Kemal Ataturk, modern Turkey’s founder, was that he was “really a Jew”. In recent years assorted leftists and Kemalists have joined an anti-Jewish chorus that frequently accompanies hostility to America, which is often accused of plotting with Israel to set up an independent Kurdish state in northern Iraq that will eventually take large chunks out of south-eastern Turkey.

Behind-the-scenes lobbying by Turkish, American and European Union diplomats may have persuaded Mr Erdogan to tone down his language. He recently told Turkey’s parliament, “As a leader, I have said that anti-Semitism is a crime against humanity.” But if anti-Israeli rhetoric in Turkey persists, the Israeli lobby in the United states could hit back by backing a congressional resolution to call the mass killings by Turks of some 1m Armenians “genocide”. Hitherto, Israel’s influential lobby in America has repeatedly helped block such a resolution, though Barack Obama and his vice-president, Joe Biden, have both referred to genocide in the past and have pledged to back the bill.

Secret talks between Turkey and Armenia to open diplomatic ties and reopen their borders are hotly opposed by some in the Armenian diaspora’s lobby in America. American Jews have long felt queasy about defending Turkey over the massacre of Armenians. Hitherto, pragmatism has prevailed and they have sided with the Turks. But if Mr Erdogan keeps on lambasting Israel, they may change their mind.

Yemen and al-Qaeda

A nice safe haven for jihadists

Jan 29th 2009 | SANA'A
From The Economist print edition

When Guantánamo closes, many of its inmates will know where to go

LAST March, al-Qaeda websites posted a message advising members to head for Yemen, the Arabian peninsula's unruly south-west corner. The call, it seems, has been answered. The global terror franchise has released a video showing fugitive Saudi jihadists and their Yemeni hosts proclaiming a merger between their two branches, plus images of combat training in Yemen's rugged mountains. Now other friends may soon be joining the fighters, by quite a different route. The Yemeni government says it expects most of the 100-odd Yemenis still held in the American prison camp at Guantánamo, where they now make up the largest national group of inmates, to be home by the spring. It is building a special camp where jihadist suspects will be allowed to live with their families, while undergoing reindoctrination to equip them for a peaceful return to society.

Yet, to the chagrin of the Yemeni and Saudi governments, as well as of an Obama administration that wants Guantánamo closed, the two Saudis in the video happen to be graduates both of the tropical island jail and of a vaunted Saudi rehabilitation programme. The Saudi authorities had freed them last year. Reunited with their families, they had benefited, as had several hundred other repentant jihadists, from state pensions designed to ease a return to civilian life. But the pair vanished a few months ago. In the video they vilify the Saudi counselling programme as a trick, and vow to pursue *jihad*. Nasir al-Wahishi, the new "emir of the Arabian Peninsula", a Yemeni, to whom they have sworn loyalty, was himself one of 23 al-Qaeda suspects who escaped from a prison in Sana'a, the Yemeni capital, in 2006.

With its rough terrain, weak central state and gun-slinging tribal culture, Yemen may prove a fairly secure redoubt for al-Qaeda. The group has suffered sharp setbacks in such places as Iraq, Lebanon and especially Saudi Arabia, where it has not mounted a serious attack since 2006. The relative quiet in Yemen, which some critics of its government ascribe to a secret amnesty whereby Sunni jihadists backed the state against a smouldering Shia insurrection in the country's north, has been eroding. Waves of arrests, prompted partly by Western and Saudi pressure, have provoked an escalation of al-Qaeda attacks that culminated in a double car-bombing of America's embassy in Sana'a last September; the attack failed to penetrate the fortified compound but left 16 people dead.

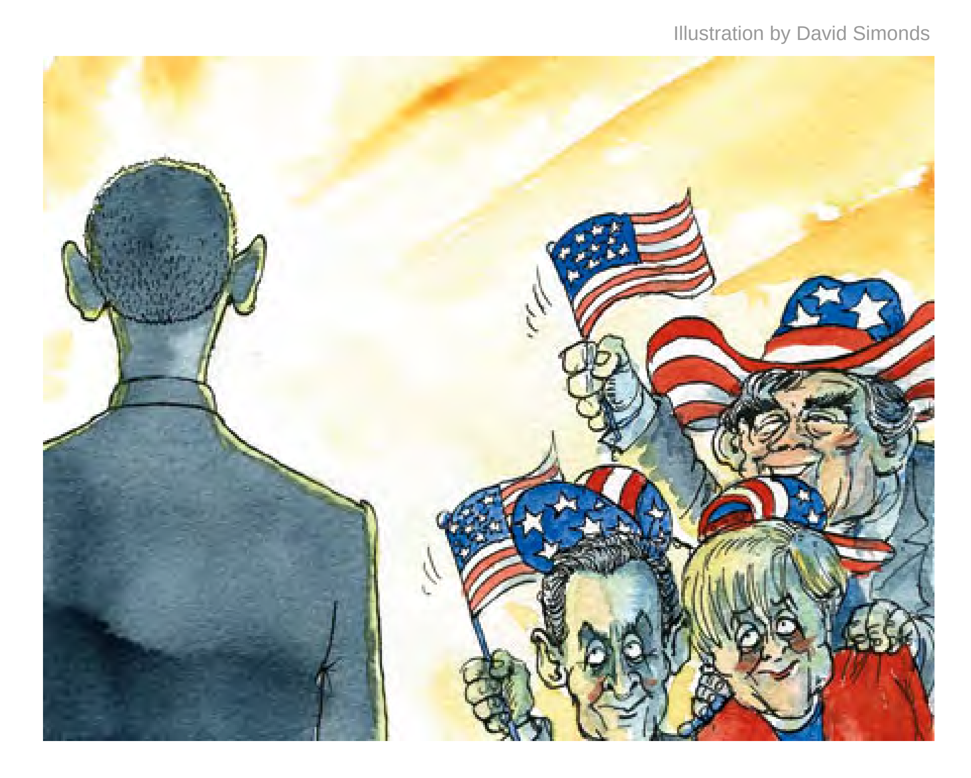
Though a Western diplomat in Sana'a describes al-Qaeda's threat there as "very severe" and the government's efforts to thwart it as merely "episodic", it is Saudi Arabia, rather than Yemen itself, that is the group's main target. The fact that al-Qaeda's Saudi branch has been forced to regroup elsewhere, under Yemeni leadership, may be a sign of weakness rather than strength. As for Yemen, even if the danger of a few hundred armed jihadists is real, locals may well care more about other national plagues: the frightening scale of corruption, poverty, malnutrition, water depletion, Yemen's plunging oil revenues, its ugly, four-year-old war in the north, simmering separatist sentiment in the south, constant tribal unrest and vicious power struggles among the ruling elite.

Waiting for the Messiah

Jan 29th 2009 | BERLIN AND PARIS
From The Economist print edition

Europe's mood of euphoria over Barack Obama masks anxiety about what the new president will demand

Illustration by David Simonds



AS THE exhilaration over Barack Obama's inauguration fades, Europeans have begun to absorb an uncomfortable truth. In his inaugural speech, the United States' new president did not mention the European Union once. Mr Obama may be at the centre of Europe's preoccupations. But Europe does not appear to be at the centre of his.

It was three days before Mr Obama telephoned a European leader. To the consternation of continentals hoping for a less British bias to transatlantic ties, the call went to Britain's Gordon Brown. Only later did he ring France's Nicolas Sarkozy, Germany's Angela Merkel and Russia's Dmitry Medvedev. By contrast, Mr Obama rang leaders of the Palestinian Authority, Egypt, Israel and Jordan a day after being sworn in. And this week he gave his first broadcast interview—to a Dubai-based Arabic television network, al-Arabiya.

European rivalry over that first call is matched when it comes to the first meeting. Despite frantic efforts (especially by Mr Sarkozy) to meet him beforehand, Mr Obama was careful ahead of his inauguration to show no favouritism. When five EU leaders turned up in Washington, DC, for the G20 summit last November, he saw none of them. "The Obama team has been very closed," says a frustrated French diplomat. Glory reflected from Mr Obama may be especially sought in Berlin, where he spoke to a huge crowd last July. The Social Democratic foreign minister, Frank-Walter Steinmeier, is challenging Ms Merkel in September's election; each would like to catch some Obama stardust.

In practice, Mr Obama's first visit to Europe is likely to be to London on April 2nd for another G20 summit. He is due a day later at a NATO summit split between Strasbourg and Kehl, a town in south-western Germany, that will mark the alliance's 60th anniversary. The Czechs, who hold the EU's rotating six-month presidency, also hope to tempt him to Prague. "Everybody wants the first visit of the Messiah," remarks one French official wryly.

Beyond all this vying for attention lies an awkward reality that might roughly be summed up as the end of the Bush excuse. As long as George Bush was in office, Europeans could throw up their hands over the

treatment of the Guantánamo Bay prison inmates but feel little pressure to take any of them in; or, indeed, to do more to help in Afghanistan. Under Mr Obama nobody will dare to seem so curmudgeonly.

The closure of Guantánamo, which Mr Obama has promised within a year (see article), has served up an early dilemma. Having called for it for years, Europeans are now divided over their response. In Brussels this week foreign ministers failed to agree. “Nobody is very warm” about taking in the prisoners, said Karel Schwartzenberg, the Czech foreign minister. Only a handful of countries have said that they would consider accepting any of the 60-odd third-country prisoners cleared for release who risk torture if they are sent back to their home countries.

France’s foreign minister, Bernard Kouchner, says he will consider requests favourably, but on a “case-by-case basis”. An especially tricky one will be Nabil Hadjarab, an Algerian captured in Afghanistan in 2001, whose family all have French passports, although he does not. His lawyer has requested that France take him. The foreign ministry seems open-minded, but the interior ministry is firmly against. Similarly in Germany, Wolfgang Schäuble, the normally pro-American interior minister, is reluctant to admit detainees. But Mr Steinmeier, normally seen as less Atlanticist, says Europe’s willingness to take some is a “question of credibility”.

Afghanistan may be still more problematic. According to the Elysée, Mr Sarkozy has promised Mr Obama that France will stand by the Americans there. He sent 700 extra soldiers last year, but has hinted that he does not plan to send any more. There is equally little prospect of many additional British troops, given the army’s current overstretch (see article).

The Germans are thus braced for Mr Obama to seek more from them. The global economic crisis will trigger a “heavy burden-sharing debate” between America and its allies, says Josef Braml of the German Council on Foreign Relations. Germany fears being asked to increase its troop numbers in Afghanistan above its 4,500 ceiling and to deploy them in more dangerous areas. Yet Mr Obama will know that the Germans are unlikely to commit more soldiers before September’s election. “The last thing the American military wants is a lot of new European troops looking for close air support,” notes Jeremy Shapiro of the Brookings Institution, a think-tank in Washington, DC.

Another awkward issue may be Iran (see article). Mr Obama has offered dialogue but also tougher sanctions to dissuade the Iranians from pursuing their nuclear ambitions. Again Germany, as the biggest Western exporter to Iran, is in the forefront. It has in the past been reluctant to accept tougher sanctions but, after an embarrassing leap in its exports last year, may now reconsider.

Mr Obama will not be able to please all. He may take a less hawkish line on Russia than Mr Bush, for example—to the relief of Germany but the consternation of central Europeans. There is speculation that he will slow the deployment of missile defences in Poland and the Czech Republic (see article). He might even consider Russia’s proposal for a new security zone stretching from Vancouver to Vladivostok, though not at the expense of NATO. Yet America’s main preoccupation in the longer run will be China, suggests Karsten Voigt, co-ordinator of relations with America at the German foreign ministry. Indeed, many in Europe sadly expect an Obama administration to focus more on Asia.

The current economic crisis may produce new transatlantic tensions, notably over trade. The Doha round of world trade talks is barely alive. Large American aid to ailing carmakers is discomfiting European governments that are under pressure to follow suit. Subsidies may indeed become a new protectionist battleground, as similar concerns play out in other industries.

In a few areas Europe may be able to offer helpful support to Mr Obama, notably the Middle East. Mr Sarkozy, who has shifted French diplomacy towards a less Arabist and more pro-Israeli position, has been characteristically busy in the Middle East recently. Mr Obama’s new envoy to the Middle East, George Mitchell, plans to visit both Paris and London on his way back from his first trip to the region.

All Europeans are relieved to see the back of Mr Bush and thrilled to have Mr Obama as president. His face continues to dominate television screens, newspapers and celebrity magazines. In the five biggest EU countries large majorities, ranging from 77% in Britain to a staggering 92% in France, told a recent poll that he would have a positive impact on international events. One struggling German firm even approached the American embassy seeking “Yes, We Can” buttons to give out to its demoralised workers.

In the circumstances the last thing any government in Europe will want is to be seen to displease the new American president. But meeting his expectations with actions, rather than fine words and rapturous applause, may yet prove hard.

Missile defence

Cool heads

Jan 29th 2009
From The Economist print edition

America is holding back its planned missile shield in eastern Europe

BELIEVE the hype, and America's planned missile-defence bases in Poland and the Czech Republic risked starting a new cold war. The Russians, claiming that they were intolerably provocative, even threatened to station new short-range missiles in Kaliningrad and to target their existing nuclear warheads at Europe. Many west European countries thought the whole affair epitomised both the Bush administration's clumsy foreign policy and the destructive paranoia of the ex-communist countries in Europe's east.

Now things are looking different. Barack Obama criticised the waste of money on "unproven" missile-defence technology during his presidential campaign. At the forthcoming Munich security conference, the Americans are expected to announce a review of the whole scheme. That could take a long time. For their part, the Russians said semi-officially this week that they would halt the planned deployment of the short-range missiles to Kaliningrad (although they are also pressing Belarus to accept new rocket bases).

On the surface, all of this sounds like good news. America hopes that Russia will come to see the missile shield as a joint project against Iran. Poland has removed a sticking-point by saying privately that it is willing to accept "intrusive" Russian monitoring of the base when it is built. Previously it had been twitchy about Russian snooping.

The new administration's willingness to talk about arms control helps as well. The main treaty dealing with long-range nuclear weapons, Start-1, expires in December. The Bush administration seemed not to care, which stoked the Russians' feeling that they were being ignored. With a decaying arsenal of nuclear warheads, and a shrinking number of ways of launching them, the Kremlin has a bigger interest in talking about cuts.

So if Russia wants a deal on missile defence, one may be possible. But what if it doesn't? American officials think the Kremlin's complaints about the scheme reflected a wish to pick a fight over Western influence in eastern Europe. Contrary to popular myth, the previous administration tried hard (albeit unsuccessfully) to present missile defences as a matter of common interest. Nobody on the Russian side could explain how a handful of interceptor rockets in Poland would hamper a nuclear superpower that can launch weapons from anywhere on the planet.

America is now committed to boosting Poland's defences. The paradox is that Russia complained loudly about something that did not matter, but by doing so it has got America to do something that does: beef up its security relationship with Poland. This will include more training and equipment (including such sought-after kit as armoured Humvees) as well as high-tech air-defence systems for Warsaw. Even if missile defences are delayed, officials say, these promises will be kept. A big theme for the Obama administration is treating its allies better.

Denmark and the euro

Nordic nerves

Jan 29th 2009 | COPENHAGEN
From The Economist print edition

Danes ponder joining the euro, Icelanders wish they could

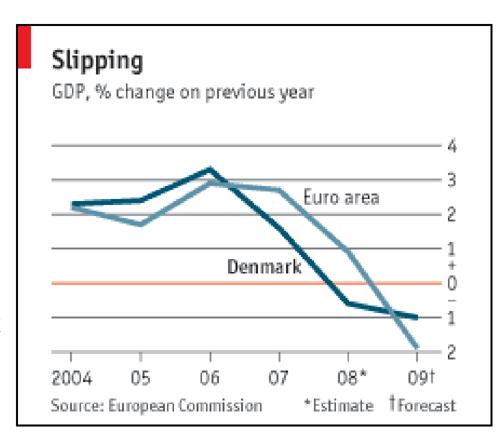
DENMARK'S story has an Old Testament resonance just now. Seven years of plenty since Anders Fogh Rasmussen became prime minister in 2001 are now being followed by leaner times. Danes hardly face seven years of famine, but jobs are being axed, property prices are plummeting and belts are being tightened everywhere. The government has already produced two bank rescue packages and it is now pondering the notion of a much larger fiscal stimulus.

Yet the gloom has not, so far, enveloped the prime minister. Unlike Iceland's Geir Haarde, who quit this week in the face of prolonged street protests, Mr Fogh Rasmussen is still seen as the safest pair of hands to steer Denmark through the crisis. A Gallup poll gives the coalition government and its far-right ally some 51.4% of the vote, slightly up on the 50.4% they took in the election 15 months ago.

Mr Fogh Rasmussen's staying power, like Mr Haarde's lack of it, has much to do with accountability. In Iceland Mr Haarde and his government were blamed as prime architects of the banking and financial crisis. In Denmark the government has successfully cast itself as David battling the Goliath of global financial turmoil. "It is well known that the international financial crisis came washing over us, as it did a lot of other countries," Mr Fogh Rasmussen said this week. He added that, thanks to prudent husbandry, Denmark is in a good position. "We used the good years to consolidate and repay foreign debt and we have the leeway to implement a crisis package should we need to."

The prime minister's belief that his government "behaved sensibly" and is accordingly without blame for the country's economic woes is not universally accepted. In Mr Fogh Rasmussen's version, interest rates in Denmark are higher than elsewhere in Europe solely because the country is outside the euro. Higher interest rates, says the government, are the inevitable cost of keeping the Danish krone.

Anders Dam, chief executive of Jyske Bank, Denmark's second-largest bank, who is anti-euro, disagrees. Higher interest rates, he says, derive from "an explosive cocktail" in which house prices rose too high because of a freeze on property taxes and the introduction of interest-only mortgages. But Mr Fogh Rasmussen rejects such criticism. The interest-rate cost is one of his two main arguments for joining the euro. The other is Denmark's loss of political influence. Voters can expect to hear him expound a lot more on both these points in the coming months.



Mr Fogh Rasmussen was a fan of the single currency long before he became prime minister; he has never hidden his ambition to get Denmark to join. In his first seven years, he never found an opportune moment to call a referendum to reverse the negative vote that Danes cast in 2000. But global economic chaos could now afford him one, and the debate has already started. If Mr Fogh Rasmussen's popularity stays high, he will have a good chance of winning a euro referendum later this year or early next (by which time a chastened Iceland may have applied for membership of the European Union as a step towards joining the euro too).

Should he manage also to orchestrate a deal on climate change at the Copenhagen climate summit in December, Mr Fogh Rasmussen will surely then have won enough kudos to secure his place in posterity—and perhaps a plum foreign job such as NATO secretary-general or, if the Lisbon treaty is ratified, the EU's first permanent president. At least he would not then have to worry about seven lean years.

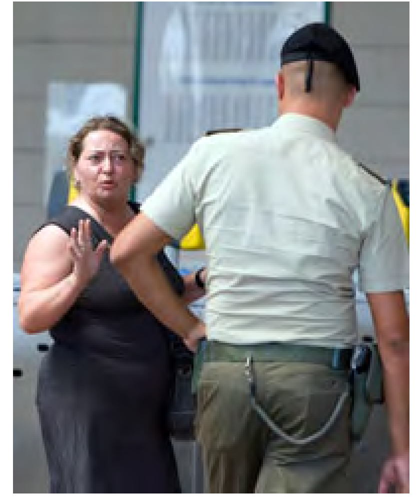
Law and order in Italy

Trouble with figures

Jan 29th 2009 | ROME
From The Economist print edition

The problems that come from promising to crack down on immigration and crime

Reuters



A soldier a day keeps crime at bay

AT THE start of the year, Silvio Berlusconi must have felt everything was going his way. Italy's right-wing prime minister was about to cure his biggest headache by selling the state's holding in a troubled airline, Alitalia. His popularity rating was high. And the main opposition group, the Democratic Party (PD), had plunged into a crisis that could yet break it up.

Yet during the past week, a black cloud has appeared on Mr Berlusconi's horizon. The law-and-order clampdown that was at the heart of his victory in last April's general election is in trouble on two fronts.

One is in the southernmost part of Italy. Lampedusa, an island 310km (about 180 miles) north of Libya, has become the main gateway into Europe for Africans fleeing poverty and war. Of the 67,000 migrants who arrived in Europe by sea last year, according to UN figures, almost half landed on this patch of sand, which is a tenth the size of Martha's Vineyard and has a resident population of barely 6,000.

Only a minority of clandestine immigrants to Italy come by sea and the government says their number is declining. But they are far more noticeable than those who quietly overstay their visas. Last year their numbers soared by 75%, embarrassing a government committed to blocking illegal immigration. In December the interior minister, Roberto Maroni, opted for deterrence. Previously migrants had been transferred from Lampedusa to Sicily, where those not given refugee status eventually received an essentially meaningless expulsion order. Some then chose to stay illegally in Italy; others moved on to other European Union countries.

Now Mr Maroni has decreed that the migrants should be held at a new identification and expulsion centre on Lampedusa itself until they are repatriated. But there are snags. One is that the new centre does not exist. After a wave of illegal landings this month, the numbers in the existing facility, which has a capacity of 850, rose to 1,800. Some detainees have been sleeping in the open under plastic sheets. The leader of a PD group that visited the site on January 23rd said he found "people crowded together in the rain, dormitories with three or four times the number who should be there and an infirmary in which the injured are piled up together".

The day after his visit, hundreds of detainees broke out of the camp and joined local people demonstrating against the government's plan. The islanders' fear, said their mayor, Bernardino De Rubeis, is that Lampedusa could become a Mediterranean Alcatraz. For another problem with Mr Maroni's scheme is that many immigrants cannot be sent home, either because their nationality is untraceable or because Italy does not have a repatriation deal with their countries. Fewer than 200 have been flown back from Lampedusa.

In so far as it reflects a tough stance on immigration, the crisis on Lampedusa is unlikely to erode support for the government. Far more threatening are events in Lazio, the region around Rome, which has seen a string of rapes. On January 27th police arrested five Romanians suspected of a horrendous gang rape a week earlier. A murderous sex attack by a Romanian in Rome in October 2007 first stirred demands for a crackdown on crime and foreigners, to which Mr Berlusconi successfully responded in the election campaign. Both voters and opposition politicians are now asking if the government's policies are working, particularly the deployment of 3,000 troops to help the police. This week Mr Berlusconi incautiously promised to increase that number tenfold, before backing away.

In characteristic style he did so with a politically incorrect quip that drew criticism even from his supporters. "We would have to have as many soldiers as beautiful women, and I don't think that would be

possible," he said. It is often the way with politics. Once trouble starts, it grows.

Turkey and the army

Conspiracy theories

Jan 29th 2009 | ANKARA
From The Economist print edition

The arrest of still more suspects in the Ergenekon case is raising new questions about the relationship between the army and the government

SOMEWHERE under the ground between the south-eastern town of Cizre and the Iraqi border lie scores of corpses of dissident Kurds who disappeared at the height of the 24-year-long separatist rebellion by the outlawed Kurdistan Workers' Party (PKK). They were tortured and murdered by counter-insurgency forces that had been given free rein in the battle against the rebels. So go the claims of a former PKK informant, Abdulkadir Aygan, who made headlines this week as he described in gruesome detail a slew of extra-judicial killings allegedly carried out on the orders of the army. A local prosecutor has agreed to investigate the charges after 47 families petitioned him to launch a search for the bodies of relatives who have been missing for years.

Mr Aygan's confessions are the latest in a series of sensational revelations unfolding in a case that takes its name from Ergenekon, a supposedly clandestine organisation. Some 86 people, including retired generals, journalists and politicians, who purportedly planned to carry out a string of high-profile murders, sow chaos and provoke a military coup in Turkey, have been on trial. Some defendants are said to have ties with the mafia and drug gangs.

On January 22nd a further 39 people (five of them serving army officers) were rounded up in pre-dawn raids across the country. These arrests have turned Ergenekon into what many say is the most significant criminal investigation in Turkey's history. The prosecutors are now exploring links with the 2007 murder of Hrant Dink, a Turkish-Armenian editor, who had been threatened by a retired general, Veli Kucuk, before his death. Mr Kucuk was arrested in January 2008 and is alleged to be among Ergenekon's ringleaders.

If the prosecution ever gets to the bottom of the case, some dark chapters in Turkey's recent past will stand revealed. And Turkey will have taken a giant step towards becoming a full-blooded Western-style democracy—and a suitable candidate for membership of the European Union. But at present the if is still big.

Since the trial began in October, claims have grown that the case is a conspiracy by the mild Islamists ruling Turkey to discredit the army. The determinedly secular generals have never disguised their distaste for the prime minister, Recep Tayyip Erdogan, whose Justice and Development (AK) Party narrowly escaped a ban by the Constitutional Court last year on charges of seeking to introduce religious rule.

The leaked diaries of a retired naval commander revealed that some fellow officers (two of whom are now in jail for alleged links to Ergenekon) had plotted at least two coups against Mr Erdogan that were blocked by the then chief of the general staff, Hilmi Ozkok. But tensions between the army and the government returned when a retired colonel shot himself dead on January 19th, after allegations in the Turkish press that he had been involved in the extra-judicial killings of Kurds. The top brass showed up in force at his funeral and in an angry statement all but blamed the media for his death. Speculation is widespread that it was pressure from the army that led to the swift release of two retired generals detained in an earlier raid on January 7th.

The Ergenekon case has become so broad and complex, and the arguments of the 2,500-page indictment so muddling, that it has left most people utterly confused. Many of those arrested still do not know what they are being charged with. Yet a recent opinion poll showed that some 60% of Turks believe in the conspiracy. Even some former prime ministers have acknowledged the existence of a shadowy network of rogue security officials and bureaucrats known as the "deep state" who will stop at nothing to stay in power. Their supposed aims include sabotaging Turkey's efforts to join the EU (not that much sabotage is needed just now: several parts of the EU negotiations remain frozen and when Mr Erdogan visited Brussels recently he left largely empty-handed).

The number of hidden weapons uncovered during the course of the Ergenekon investigation has bolstered

claims that the gang meant real business. In early January a map found at a leading suspect's home in Ankara led police to an arms cache that included 300 bullets, 700 grams (1.5lb) of plastic explosives and two anti-tank weapons. Further searches have yielded bombs and other equipment.

The growing body of evidence has embarrassed the generals. It has also exposed divisions within the army, pitting anti-Western soldiers who favour closer links with Iran and Russia and are known as "Eurasianists" against those committed to Turkey's friendship with America and its putative membership of the EU. The second group includes General Ilker Basbug, who is now the chief of the general staff.

The desire to weed out the Eurasianists may explain the army's silence in the face of the arrests of serving soldiers who have been implicated in the Ergenekon case. It may also explain the apparent truce that has been struck between Mr Basbug and Mr Erdogan, who have recently agreed that they should hold weekly consultations.

The worry is that the price of any compromise between the army and the government may be to let some of the high-ranking officers thought to be involved in the conspiracy off the hook. An opportunity to assert civilian control over the army once and for all would then have been missed. For Turkey's reputation in the West, especially in Brussels, much is riding on the outcome of this case.

Charlemagne

An Iranian conundrum

Jan 29th 2009
From The Economist print edition

Europeans fret that this year will be the trickiest so far for dealing with Iran

Illustration by Peter Schrank



IF COUNTRIES like Iran are willing to unclench their fist, Barack Obama said this week on Arabic television, they will find an “extended hand” from America. You might expect Europe to react with a fresh outburst of Obamamania. After all, Europeans like to talk. The European Union, represented by its diplomatic big beasts—Britain, France and Germany—has spent years, together with Russia and China, talking to Iran, in a bid to curb its nuclear ambitions with a set of sticks and carrots.

On the campaign trail, Mr Obama talked of “bigger sticks and bigger carrots” for Iran. This meant direct diplomacy between America and Iran, after three decades of near-silence. But it would be matched by tougher sanctions, for example on Iranian banks that finance uranium enrichment (an activity Iran says is peaceful and aimed at generating electricity one day, but many others believe to be a scheme to build a bomb).

Yet the European response to Mr Obama over Iran has been mixed. Senior diplomats from the 27 EU members discussed Iran in Prague in January. France (a hawk) proposed adding two Iranian banks to the sanctions list. If the EU wanted to remain “relevant” for the Americans, the French representative told his colleagues, it had to be ready to carry a “bigger stick”. Then came the objections. Some fretted about hurting ordinary Iranians; others preferred to wait for a request from Mr Obama; others still wanted sanctions agreed by the UN Security Council, to ensure that Russia and China were on board. They have a point: a drop in EU trade with Iran since 2005 has been offset, almost euro for euro, by rising Chinese sales to Iran, undermining the sanctions.

Even so, existing sanctions are having an impact on Iran’s economy “at rather important margins”, insists a diplomat. With oil prices still low, Iran’s economy is in deep trouble. Nor are all objections to sanctions disinterested. Under pressure from governments, French, British and Spanish energy firms have frozen investments in Iran. Others have been less fussy. OMV, Austria’s big energy group, has invested heavily in Iranian onshore oil, and also has a draft agreement to explore for natural gas. German businesses are leading exporters to Iran: November’s figures showed that German exports to Iran had actually grown by some 10% over the previous year.

And yet when it comes to Iran, most EU members do not matter much. Only a few countries have the intelligence and diplomatic resources to focus on the threat from Iran. Talk to them alone, and the prospects for co-operation between Europe and America look brighter. Gruff policy types in America may grumble that Europeans appear more worried about a pre-emptive Israeli strike on Iran than by the prospect of an Iranian bomb. But in fact either prospect fills Europeans with horror—and that is enough. To quote the French president, Nicolas Sarkozy, serious diplomacy is the only means of avoiding a “catastrophic” choice: “an Iranian bomb or the bombing of Iran”.

The EU3 of Britain, France and Germany are realistic about the talks they, along with the EU’s foreign-policy chief, Javier Solana, have held with Iran. Europe has a “very good policy” for curbing Iran’s nuclear ambitions, says a diplomat, dryly; the problem being that it has not worked yet. The Europeans also accept that any final deal will be struck by America and Iran. They stepped in only because America was not available. Russia goes along with today’s sanctions out of “despair”—objecting to the policy, but having nothing else to offer. China is torn between its need for energy security and its dislike of nuclear proliferation.

All sides see this year as decisive. Iran is expected to pass a threshold in the second half of 2009, amassing enough low-enriched uranium to get close to a bomb, though it would still need to enrich it to higher levels to fuel a nuclear device. Once that threshold is crossed, diplomacy becomes harder (though a sprint for a bomb would be risky, as it would be visible and the enrichment process would take several weeks). And from now on American engagement will be crucial, too.

Last tango in Tehran

A senior diplomat says that Iranian envoys have spent the past few years “playing for time”. EU negotiators spent hours answering tangential questions, and listening to declarations about the greatness of the Persian people—“going back to Cyrus the Great”, he sighs—leading up to its right to civilian nuclear technology. Some argue that Iran’s supreme leader, Ali Khamenei, has never really been willing to negotiate in earnest. A top Khamenei aide, Ali Akbar Velayati, met Mr Sarkozy secretly in November 2007, but the initiative fizzled.

France and Britain take Iran very seriously; and after an ambiguous few years, Germany is now almost as tough. Angela Merkel, the German chancellor, has faced down the economics ministry (and some in the foreign ministry) to curb export-credit guarantees for firms trading with Iran. Under Silvio Berlusconi, Italy backs tough sanctions, despite its energy ambitions in Iran.

European, Russian and Chinese diplomats handling the Iran dossier will meet William Burns, their American colleague, in Germany next week to discuss strategy. The Europeans will urge the Americans to engage, but prudently. Some feel that America should not talk to Iran before the Iranian presidential election, for fear of handing a propaganda coup to Mahmoud Ahmadinejad, who is running for re-election. Others disagree, urging immediate talks. All say that American engagement is a trump card, to be played with “circumspection”.

At the least, if an extended American hand is brushed aside, some “pretty chunky” UN sanctions will be needed. And, if American diplomacy fails completely, only bad options will be left. Europe’s biggest powers are willing to do much to avoid that outcome, and they are the ones that count. On Iran, the transatlantic powers see pretty much eye to eye.

Britain's armed forces

Losing their way?

Jan 29th 2009
From The Economist print edition

AFP



The British army suffers from lack of soldiers, lack of money and lack of conviction

SOME marched smartly down the high streets of garrison towns, to cheers from bystanders waving union flags. Some, wounded, stood uneasily on crutches to receive decorations in their parade squares. Many went to church to give thanks for their safe return and remember fallen friends. For the men and women of 16 Air Assault brigade, returning from their latest tour in Afghanistan, the past months have been a homecoming like few others. There will be more cheers this summer when British troops come back from Iraq for good. On June 27th Britain will begin to mark a new Armed Forces Day.

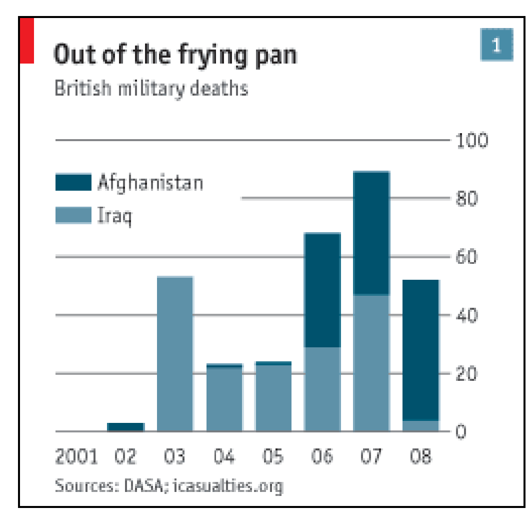
British forces have been at war for the past seven years. But it is only recently that, following the example of American parades, the public has been encouraged to honour them. Such displays are a surprise to many soldiers who, for decades, were largely hidden from view in Britain, coming out of their barracks in civvies in order to avoid attack by the Irish Republican Army (IRA). Television documentaries and a quick-fire burst of books with titles such as “3 Para: Afghanistan, Summer 2006. This is War” have also publicised the deeds of Britain’s fighting men and women. Despite the qualms about Iraq and Afghanistan, and instances of soldiers being abused, support for the troops is high. According to an Ipsos MORI poll published in November, 81% of Britons regard them favourably; most agree with their prime minister, Gordon Brown, that Britain’s armed forces are “the best in the world”.

But are they? For all the public recognition, the armed services are going through unusually difficult times. This is challenging Britain’s belief in itself as a fighting nation with an important role in the world. The severe strain of waging two wars in faraway countries has been aggravated by undermanning and equipment shortages. More serious still is a new mood of self-doubt. The invasion of Iraq was controversial and its occupation inglorious; the campaign in Afghanistan is going badly. British commanders have belatedly realised that they have much to learn, or rather relearn, about fighting small wars in distant lands. “We have lost our way,” says one general.

Underlying this malaise is concern about Britain’s relationship with America, its most important ally. Generals worry that the United States is losing confidence in Britain’s military worth. Some Americans have indeed been expressing doubts: policymakers ask whether British leaders are losing the will to fight, soldiers whether their British counterparts are losing the ability to do so. There is talk that Britain is becoming “Europeanised”, more averse to making war and keener on peacekeeping. Britain remains America’s closest and most able ally; its special forces are particularly prized. But one senior official in the former Bush administration says there is “a lot of concern on the US side about whether we are going to have an ally with the capability and willingness to be in the fight with us”. He is bemused by the “tyranny of the lawyers” who constrain British military operations and dumbfounded by how “you only see British officers wearing their uniforms when they come to visit Washington, not in London.”

Jack Keane, a former vice-chief of the American army and a

driving force behind the surge that sharply reduced violence in Iraq, reckons the relationship with Britain has "frayed" over recent years. Ordinary soldiers are blunter: a popular quip among Americans in Afghanistan is that ISAF, the NATO-led International Security Assistance Force in Afghanistan which prominently includes the British forces, really stands for "I Saw Americans Fight". After the death of 320 British soldiers in America's "war on terror" (see chart 1), such jokes are especially wounding.



This change of mood is striking. The British may have less military brawn than America, but they have prided themselves on often having more brain; with a history of empire and the experience of Northern Ireland, British soldiers saw themselves as masters of that particularly messy kind of warfare from peacekeeping to counter-insurgency—"war among the people", as some put it. In the early days in Iraq, British soldiers patrolled Basra as they did Belfast: on foot and wearing soft berets. They were aghast at how the Americans, by contrast, tore around Baghdad in armoured vehicles, obsessed with "kinetic" operations to kill and capture enemies. This is, of course, something of a caricature. The Americans were operating in a more hostile area, and British soldiers too would have to don helmets as Shiites later turned violent in Basra. Still, as American commanders struggled to stop Iraq's spiral into civil war, Mr Keane was among those who pushed for the British to move into central Iraq in order to help the Americans do a better job.

Putting the boot in

In 2005 a British brigadier, Nigel Aylwin-Foster, penned a critical analysis of the American army: he accused its soldiers of cultural ignorance to the point of "institutional racism"; of having a "predisposition to offensive operations"; and of displaying a "moral righteousness" that could "distort collective military judgment". His controversial reproach had the support of influential Americans who wanted their army to learn the art of counter-insurgency that it had abandoned after Vietnam.

Three years on, however, the same people think it is time for American commanders to speak out about Britain's shortcomings. It has not yet come to that. But Daniel Marston, an American military historian who taught at Britain's military academy, Sandhurst, hit a nerve when he said last summer that British policy was "close to humiliation" in Iraq and "almost destroyed" in Afghanistan (although Britain has latterly performed better in both).

David Kilcullen, until recently a counter-insurgency adviser to the American government, says both America and Britain misunderstood Iraq: America thought it was dealing with a terrorist problem rather than an insurgency; Britain thought its job was peacekeeping rather than imposing control. The subsequent bloodbath pushed the allies in opposite directions. Britain gave up the fight, cut a deal with militias terrorising Basra and got out of the city centre where soldiers were dying almost daily. As the junior allies, British officers felt they could do nothing in Basra to change the course of a war being lost, they thought, by American troops in Baghdad.

But American forces could not bear another Vietnam-style defeat. In 2006 they wrote a counter-insurgency manual that drew partly on Britain's colonial wars. Its watchwords were "clear-hold-build": clear an area of insurgents, hold on to the gains rather than move on, and build up government and the local economy. General David Petraeus, the doctrine's leading proponent, was sent to Iraq with more troops to put it into practice, to striking effect.

The result was that, as the Americans were building up in Iraq in 2007, the British were drawing down (ostensibly to give Iraqis space to find their own solutions). If Tony Blair had misread the problems of occupying Iraq, his successor as prime minister, Gordon Brown, misread America's determination to put them right. Matters came to a head last March, when the Iraqi forces unexpectedly moved to retake Basra. Their troops took a beating at first, yet the British stood aside (their commander was away skiing). The Americans then helped win the day by sending their troops, training teams embedded in Iraqi units and a separate headquarters. It took five days for the British to change course and insert their forces into Iraqi units too (as they had done previously).

To many Americans, "Charge of the Knights", as the operation was known, exposed the failure of the British; to others it showed their readiness to adapt. Either way, it saved British face, allowing Mr Brown to announce in December the withdrawal of the remaining 4,100 British troops and claim, plausibly

enough, that “we leave Iraq a better place.” One British general puts it differently: “We are lucky that just as we were getting tired the Americans decided to change their strategy.”

Britain’s slow retreat from Iraq was justified, in part, by the need to concentrate on Afghanistan. But here, too, the British have had acute problems. When their troops deployed to Helmand in 2006, 16 Air Assault brigade was parcelled out in “platoon houses” across the province. Paratroopers fought pitched battles against the Taliban. The British later withdrew from an outpost in Musa Qala, in theory ceding control to loyal tribal elders; instead, the Taliban took control. Once again it was the Americans who led the way in retaking the town in December 2007, deploying a battalion alongside Afghan and British forces.

Basra and Musa Qala—not to mention the capture of British sailors and marines at sea by the Iranians in March 2007—have fed American worries about British forces. In the absence of an updated counter-insurgency doctrine of their own, British officers have been using General Petraeus’s manual. Other factors too conspire against the development of a coherent plan of action. British troops rotate every six months (American army units every 12, down from 15), and change tactics endlessly. The first brigadier in Afghanistan fought pitched battles in fixed positions; the next favoured raids through the desert; another preferred to keep sweeping through the same areas without holding them. Some Americans complain that British troops are too quick to ask for air strikes; British officers accept that American ground forces have more fighting power, and are often more daring.

Sir Jock Stirrup, the chief of the defence staff, says “there is nothing wrong” with allies operating in different ways but he admits Britain had become “too complacent” and “smug” about its experiences in Northern Ireland and Bosnia. “You’re only as good as your next success, not your last one,” he says, but things are being put right: new doctrine will be published this year and key staff will serve longer tours.

There is a sense that the American student has surpassed the British master. But the lessons are not all one way. General Petraeus recognises that the first contacts with Sunni tribes in western Iraq, which led to the “Anbar Awakening” that drove out al-Qaeda, were led by a British general, Graeme Lamb. He helped win over American sceptics by recounting how he had overcome his own revulsion at dealing with the IRA for the sake of peace. A second innovation started in Afghanistan and exported to Iraq—the creation of military-led provincial reconstruction teams to build up the local government and economy—was the brainchild of a British colonel (now major-general), Nick Carter.

Britain’s shortage of men and firepower, coupled with a different level of political commitment (“The Americans are at war, but we are on operations,” one British officer says), goes some way to explaining why the British have been inclined to limit their ambitions. Yet the relationship with America is central to Britain’s defence policy and position in the world. Its military forces are designed, in part, to maintain its influence with America and its place at the international top table: powerful enough to be taken seriously and ready to fight on “day one” of a war alongside America. This means having a nuclear deterrent, a deployable army division, a blue-water navy with two aircraft carriers, and an air force with fighters and deep-strike jets.

Defence ties with America bring big benefits: intelligence is shared and Britain has preferential access to some American technology, not least the Trident missiles that help make Britain’s nuclear deterrent cheaper than France’s. But close ties bring dependence and obligation. In 2002 Mr Blair accepted that Britain had to pay a “blood price” for this special relationship. At moments of crisis, he said, America had to know that Britain was “prepared to be there when the shooting starts”.

British forces are organised to conduct, at the high end of operations, either one relatively brief “large-scale” war (requiring an army division, or about 30,000 men) or two simultaneous “medium-scale” campaigns (brigade-sized, involving around 4,500 men apiece). In the latter case, one operation could be a long-term peacekeeping mission and the other a short war; they would not both last longer than six months or involve prolonged combat.

But since 2006 Britain has run two protracted and often intensely violent operations. Units routinely breach guidelines designed to give them time to minimise battle stress. The strain on soldiers, says General Sir Richard Dannatt, the army chief, is “unacceptable”. Britain has struggled to maintain two long supply routes, dividing scarce helicopters, engineers and medics. Aircraft are wearing out faster than planned. “The British army is like an engine running without oil. It is still going, but it could seize up at any moment,” argues Michael Clarke, director of the Royal United Services Institute, a think-tank.

These troubles are made worse by a chronic shortage of manpower. On October 1st the trained strength of the British armed forces was 173,270. This is 3.2% below the official requirement, but it understates large gaps in some areas—especially infantry units. Most battalions are 10-20% short of their required

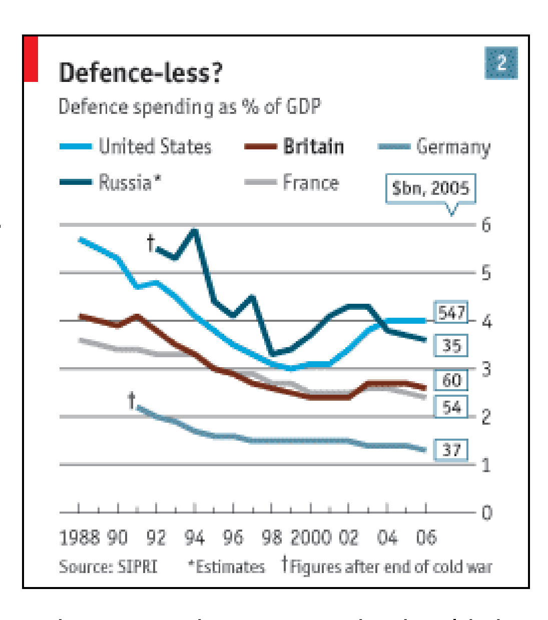
numbers; if those deemed unfit to deploy (due to, say, battle injuries) are factored out, they are as much as 42% under strength. So when battalions are preparing for war, they often regroup soldiers from their four scrawny companies into three, and then bolt on a fourth from another unit. To support current operations, the army has cut back training and lowered readiness; instead of having roughly a brigade at high readiness to deal with a crisis, sources say, there is “less than a battle-group” (a 1,500-strong formation).

Withdrawing from Iraq will relieve some of the strain. But operations in Afghanistan alone, involving some 8,000 British troops, arguably are already more demanding than the structure permits—and many expect Britain to send another battle-group to support the American reinforcement there. Generals want the army to grow. Yet it struggles to recruit, train and keep enough soldiers to fill its existing quota. An acute problem is the large “wastage” of recruits. Last year 38% of those in training either gave up or were thrown out—a bigger share than in the American army. Britain gets by in part thanks to foreigners: Commonwealth citizens (who made up more than 6% of soldiers in 2007), Irish recruits and Gurkhas. The top brass hopes the recession will encourage more to join and fewer to leave. But more soldiers cost more money, and that will be in even shorter supply in a downturn.

Plainly, Britain’s military resources do not match its commitments. Three ex-generals have said that Britain’s “unusable” nuclear weapons should be scrapped. But Sir Jock reckons that any money saved would almost certainly go back to the Treasury, not the conventional forces.

On December 11th the government announced a delay of one or two years in building big new aircraft carriers, and the deferral of a new family of armoured vehicles. Even so, insiders say there is still a £3.7 billion ($5.2 billion) hole in the budget for military equipment over the next four years and procurement costs are still rising. The bill for the 20 biggest weapons projects is now £28 billion, or 12%, over budget.

Heavy spending on kit for the navy and air force leaves little for the army; one source says it will receive less than 10% of all spending on defence equipment between 2003 and 2018. The government notes, however, that better-protected transport vehicles and other things are being rushed in separately using the Treasury’s reserve funds; the force in Afghanistan is now the best-equipped that Britain has fielded (though it still trains with old kit).

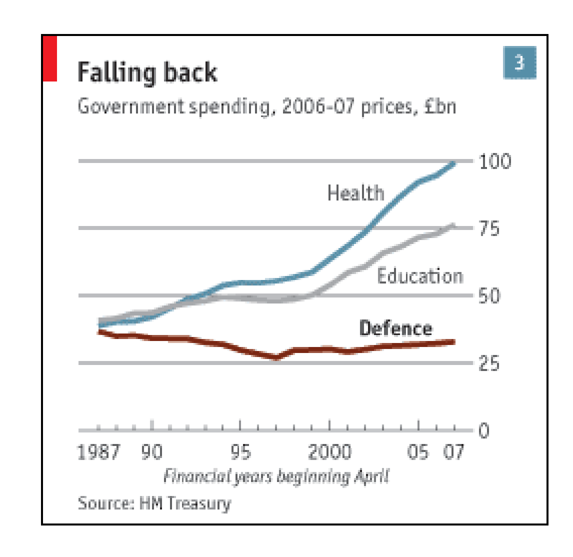


How much should Britain spend on defence? At around 2.6% of GDP, its defence budget is high by European standards but below America’s 4% (see chart 2). Defence spending has lagged behind other government expenditure (see chart 3). One general says: “You cannot have a first-division army, navy and air force—and a nuclear deterrent—for £34 billion a year.”

The test of Afghanistan

Britain badly needs a wholesale review of its defence policy. Two questions must be answered. Should the British continue to aspire to a global military role? And what sort of wars is the future likely to bring? If it is long messy ones like the fight in Afghanistan, the structure and equipment of the armed forces must change. One general complains: “We are acting as if Afghanistan is just an aberration. We are in huge danger of preparing for the wrong war.”

The stakes for Britain are high, not least in terms of its relationship with America. Barack Obama, the new president, plans to send up to 30,000 more troops to Afghanistan. The British will be scrutinised, especially when a British general takes overall command in the south this autumn. Some British officials think the Afghan mission is hopeless: better to start extricating Western troops than to redouble the military effort. But others, especially in the army, insist Britain must do a better job. “We have to prove to the Americans and the other allies that we are still a capable nation militarily,” says one general. The army may like the homecoming parades, but it has no desire to stay at home for good.


Falling back
Government spending, 2006-07 prices, £bn
3
Health
Education
Defence
100
75
50
25
0
1987
90
95
2000
05
07
Financial years beginning April
Source: HM Treasury



Rescuing carmakers

Mandy's promise

Jan 29th 2009
From The Economist print edition

A well-intentioned package arrives little and late

IF Gordon Brown, the prime minister, claims that he saved Britain's banking system, can Lord Mandelson, his business secretary, style himself the saviour of its car industry? On January 27th he announced a £2.3 billion ($3.2 billion) package of loan guarantees to support carmakers, the development of clean low-carbon cars and the skills to produce them. Another scheme, yet to be devised, will aim to stimulate demand by helping finance companies that lend money to buy cars.

Opposition leaders described the whole as "pretty small beer" and unlikely to prevent the loss of jobs and expertise. As elsewhere, car sales and production have tumbled. Nissan has said 1,200 jobs will go in Sunderland, and Jaguar Land Rover (JLR) has cut 450 (in addition to 850 in November); Honda in Swindon and Bentley in Crewe have suspended production for over a month. Overall, 850,000 jobs depend directly on the car industry.

Up to £400m of the package, say some, is aimed at JLR, which has been asking for £900m in government money to finance working capital and the transition to low-carbon cars. JLR is owned by the Indian Tata group, as is Corus, a steelmaker, which on January 26th announced a restructuring that may cost 2,500 British jobs. As intra-group financial flows are hard to monitor, Lord Mandelson's package has been cheekily dubbed "the Indian takeaway".

The biggest slice of guarantees will support up to £1.3 billion of lending to firms by the European Investment Bank. Insurance for another £1 billion of British bank lending will target car companies with turnover greater than £25m that offer green or advanced technology, or foster especially valuable skills. A further £85m is aimed at training car-industry employees.

For the second leg of the rescue, Mervyn Davies, recently appointed minister for trade and investment, is trying to get car-purchase credit flowing again. America has pumped money into the financing arms of Chrysler and General Motors; Germany has offered to guarantee borrowing by the financing operations of its big carmakers; France's firms have been offered up to €6 billion (£5.6 billion) of state funding if they keep their French factories open. Germany and France have also promised cash bonuses to buyers of new green cars who scrap their old ones. But in Britain some 85% of the cars bought are imported, so such bribes might not do much for local carmakers. And car purchases are financed mostly by small non-banks, an awkward channel for state aid.

Lord Mandelson's package will not immediately unlock bank funding and is unlikely to meet urgent needs. Magal Engineering of Reading may see its workforce dwindle from 1,000 to 250 for want of bank credit, said David Woolford, its chief operating officer, at a car-industry meeting. The main alternatives to banks for firms in search of help in a hurry are England's nine regional-development agencies. A fund attached to the one in the West Midlands can release up to £250,000 quickly, but at six to eight percentage points above the base lending rate. Lord Mandelson may have shown his concern for the motor industry, but those in the sector fear that his modest help will arrive too late to save any but JLR.

Scottish politics

Budget show-stopper

Jan 29th 2009 | EDINBURGH
From The Economist print edition

The nationalist government begins to look vulnerable

AFTER ruling Scotland pretty much as he pleased since winning power in May 2007, the nationalist first minister, Alex Salmond, crashed into a roadblock this week. On January 28th the Scottish Parliament rejected his budget for the coming fiscal year. Mr Salmond promptly presented it again, indicating that he would resign and hope to force an election if he did not win on a second vote. So do farewells loom for the independence-minded leader?

Not necessarily, and certainly not yet. The arithmetic of minority government in the 129-seat Scottish Parliament is complicated. Mr Salmond's Scottish National Party (SNP), with only 47 votes, has to win either Labour's 46 votes or backing from two smaller parties to secure the 65 votes needed for a majority. That is why the SNP, though it agitates for a referendum on Scottish independence, has steered clear of real controversy in legislating, proffering crowd-pleasing measures such as an end to hospital car-parking charges instead.

The one thing Mr Salmond cannot finesse is the annual budget vote. This year he secured the 16 Conservative votes by promising £60m ($86m) to regenerate town centres. More cash for housing won the sole independent, Margo MacDonald.

But he seems to have taken for granted the support of the two pro-independence Greens. They asked weeks ago for £100m a year over ten years to finance home insulation, and were outraged to be offered £22m at the last minute for a pilot project. They voted against the budget. With the ballot tied at 64-64, Parliament's presiding officer, Alex Fergusson, followed convention and cast his vote against the new measure.

This stand-off may be as much about parliamentarians asserting their rights as it is about spending decisions. In recent months all opposition parties have grown angry at the way the government's reliance on executive action has sidelined the legislature. Two weeks ago Tavish Scott, leader of the Scottish Liberal Democrats, complained of an apparent inaccuracy in an answer given to him by Mr Salmond. Mr Fergusson acknowledged MSPs' frustration and promised an inquiry into the "veracity" of ministerial responses.

The vote also reflects a growing sense of SNP weakness. Mr Salmond's threat to quit if his budget is again defeated does not carry the weight it used to. While his populist style lifted the SNP's poll ratings, no party dared challenge him. But since November, when a Westminster parliamentary by-election in Glenrothes produced a comfortable Labour win instead of the expected SNP victory, he has looked a lot more vulnerable. And dire economic figures released on January 28th suggest that Scotland's plunge into recession may be steeper than that of Britain as a whole, which casts doubt on the SNP's claim that Scotland would be better off on its own.

A new budget must be passed about six weeks before the start of the new fiscal year in April, or spending will fall back to current budget levels. Everyone will want to avoid that outcome. But Mr Salmond's resignation need not force an election. It is up to Parliament to choose the first minister and it could well select someone from another party, perhaps as head of a coalition pledged to see Scotland through the economic crisis. Tense times ahead.

Tidal power

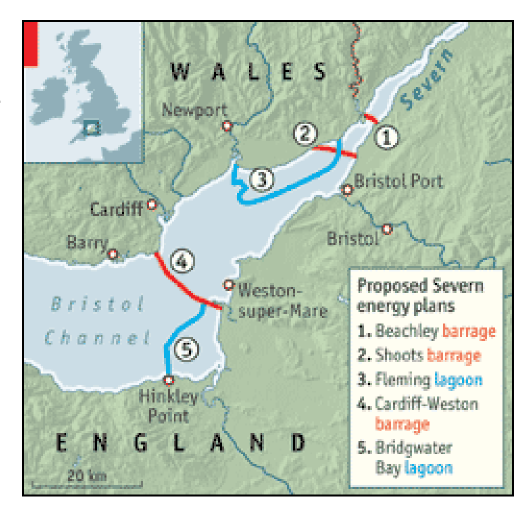
Green on green

Jan 29th 2009
From The Economist print edition

Environmentalists square up over an ambitious tidal power plan

FOR all its stirring rhetoric, the government's record on renewable energy is poor. Geographically, Britain is ideally placed, enjoying (or enduring) some of the windiest weather and heaviest seas of any European country. Yet in 2005 (believe it or not, the most recent year for which comparable figures are available) Britain got less than 2% of its energy from renewable sources (mostly wind). This was considerably below the European average of 6.7% and far behind countries such as Denmark (16.2%) or Sweden (29.8%).

One single project could provide an enormous boost. The river Severn, Britain's longest, which flows from Wales to the Bristol Channel, has a tidal range of 15 metres, the second highest in the world. Engineers have long fantasised about harnessing all that energy, and with climate change and energy security now pressing political problems, ministers are taking them seriously. On January 26th the government published a shortlist of possible projects, including three barrages (essentially gigantic dams) and two tidal lagoons (man-made tanks in the sea which fill up and empty with the tide).



It is easy to see the attraction of such schemes. Tidal energy is the best-behaved of renewable sources. Unlike wind or wave power (or even hydroelectricity, which depends on the rain), tides—governed by the immutable laws of celestial mechanics—are predictable. The sheer size of some of the plans are impressive too. When the tide is flowing fastest, the biggest option—a ten-mile, £22 billion barrage running from Weston-super-Mare to Cardiff (see map)—could generate 8.6 gigawatts, around a seventh of Britain's peak consumption and more than every other renewable-electricity source combined. Although its average output would be far below its peak, it could still supply around 5% of Britain's electricity every year.

Such a scheme could put a noticeable dent in British carbon emissions, but greens concerned about the local environment are unhappy. The Severn estuary is an important habitat for birds; large barrages would destroy or damage much of it, as well as interfere with fish stocks in the river. Friends of the Earth, an environmental lobby group, thinks offshore lagoons might be a useful compromise.

Others object on economic grounds. Ministers admit that the biggest proposal would require taxpayer funding. A report by Frontier Economics, a consultancy, argues that the same amount of renewable power could be obtained more cheaply with other technologies such as wind turbines. A barrage could affect shipping into Bristol, a big port. Some simply think it would be an eyesore.

A final decision on what project to go for and when is at least a year away. The Conservatives (who may well be in power when it is taken) say they are not opposed; yet even if construction went ahead it could hardly be finished until after 2020.

But there are other reasons too for politicians to support the project. Like the Hoover Dam, built at the height of the Great Depression in America, a Severn barrage, the British government claims, could create tens of thousands of jobs and lots of work for firms. And as one of the world's largest engineering projects, it would, of course, be a long-lasting monument to whichever politician approved it.

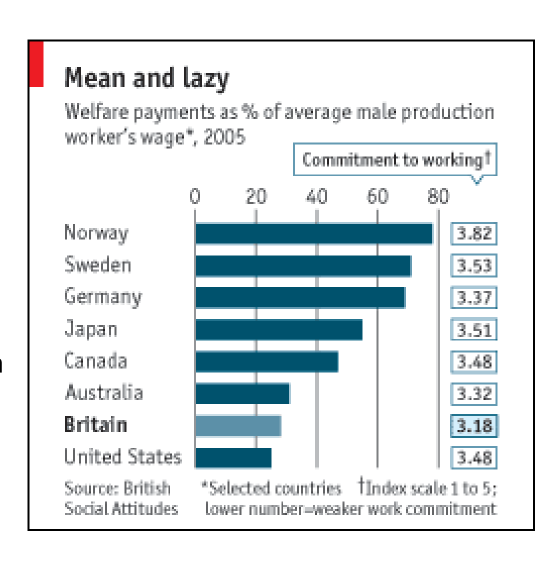
Attitudes to work

Can't? Or won't?

Jan 29th 2009
From The Economist print edition

An ungenerous state—and an unmotivated populace

THAT mythical beast, *homo economicus*, is utterly clear about the purpose of work: to get paid. He is keener on leisure than on work, and if money can be got without effort, he downs tools. If real people feel the same, then bountiful out-of-work benefits should be found in the same places as work-shy citizens.



Yet a cross-country comparison of benefits and attitudes to work published on January 28th finds precisely the opposite pattern. Researchers ranked 13 countries according to their generosity (measured by comparing typical benefits to those out of work with the average wage of a production worker) and their citizens' commitment to work (gauged by asking whether they would work if they did not need the cash, and whether they regarded a job as merely a way to earn a living). The more generous a state is, the keener on work its people are, they found (see chart). Britons, whose benefits were the stingiest after those that Americans get, were least keen of all on work.

One reason may be the skills make-up of the British workforce. The researchers found, logically enough, that professionals and graduates were more positive about work than the unskilled and non-graduates. Fewer Britons than Norwegians (who came top on work commitment) have professional jobs or degrees. But this does not entirely explain their comparative immunity to the attractions of toil: Britons of every social class and level of education were less keen on work than their counterparts elsewhere.

Could the “dependency culture” currently exercising British politicians be solved by raising benefits? Unlikely, says Alison Park, editor of the annual British Social Attitudes Report, in which the study appeared: attitudes to work vary from country to country for many reasons. The lavishness of what the report terms “encompassing” states, all Nordic with Lutheran traditions, may have been made possible by a strong work ethic, rather than a stronger commitment to work having emerged as a result of it.

And work incentives are affected by features of welfare systems other than overall generosity: “corporatist” states such as Germany, which pay higher benefits to those with a longer work history, may be encouraging positive attitudes to work by such conditionality. Britain's meagre benefits, by contrast, are largely independent of previous employment, which may mean they are seen as an alternative to work, rather than as one of the good things that flow from it.

Parliamentary sleaze

Ermine-gate

Jan 29th 2009
From The Economist print edition

The Lords catch the MPs' scandal bug

FOLLOWING a newspaper investigation published on January 25th, the "dignified" part of the British constitution now looks anything but. Journalists posing as lobbyists for a fictitious Hong Kong firm interested in opening a chain of shops in Britain approached ten members of the House of Lords for help in amending business-rates legislation. They were given short shrift by three Conservatives, one Liberal Democrat, an Ulster Unionist and a Labour lord, but four other members of the governing party—Lords Moonie, Snape, Taylor and Truscott—seemed willing to help in some degree in return for retainers of up to £120,000 a year.

Members of both chambers are forbidden from "exercising parliamentary influence" in return for money. Loopholes abound, however, and peers are allowed to act as paid consultants. All four in this case deny wrongdoing, and two inquiries by the House of Lords have yet to report. But as alarming as the allegations against them is the dearth of punishments available if the men are found to have breached the rules. Unlike MPs, lords cannot be expelled or even suspended.

Westminster is used to the spectacle of the lower house embroiled in financial scandal; earlier this month Jack Straw, the justice secretary, and Peter Hain, a former cabinet minister, were reprimanded for failing to declare donations as required. But the unusual characteristics of the second chamber make it, in theory, even more susceptible to graft: its members are unelected and mainly serve for life, and they receive expenses but no salary, prompting many to pursue outside income. Nostalgics say this was compounded by the removal of most of the independently wealthy hereditary peers in 1999—though few espouse the cause of restoring that aristocratic privilege now.

Indeed, the latest scandal is brandished by some as proof of the need to complete the government's decade-old project to overhaul the Lords, not to tinker with it. That peers are offered money to change legislation shows they are more powerful than the caricature of an ornate revising body suggests. MPs voted for a fully elected second chamber in 2007, though this was rejected by the Lords themselves.

Others, such as Meg Russell of University College London's Constitution Unit, say incremental reforms have usually fared better than radical ones. Allowing lords to be dismissed from Parliament would be a start, and it has cross-party support. Strengthening the independent appointments commission to make it tougher for the prime minister to stuff the chamber with party placemen would be another quick win. Bolder moves, such as fixed terms and the vexed question of elections, can be revisited later.

Too much change may also threaten the virtues of the second chamber, say those impressed by the expertise and independence on show there. Ms Russell agrees that it has improved unrecognisably over the past decade; more than a third of its members are new since the days when hereditary peers dominated a cowed and quiet institution. Dignified rather than effective, Walter Bagehot, a former editor of *The Economist*, called the Lords a century and a half ago. A modern assessment might put it the other way around.

A new chief policeman

'Ello 'ello 'ello

Jan 29th 2009
From The Economist print edition

Continuity prevails as the deputy takes charge of the Metropolitan Police

FROM odds-on favourite to no-hoper and back: Sir Paul Stephenson at last settled into the commissioner's office at New Scotland Yard on January 28th after a bumpy candidacy. In October, following the forcing out of Sir Ian Blair, the Met's previous chief, the smart money was on his steady deputy Sir Paul to succeed him. But when in November officers acting on Sir Paul's authority carried out a bizarre raid on the offices of Damian Green, a shadow minister who had received a series of Whitehall leaks, his campaign looked sunk. Why the miraculous recovery?

Most straightforwardly, the cock-up failed to eclipse an otherwise good 35 years in uniform, including a spell in Northern Ireland and nearly four years as number two in the uniquely big and complex Met, a job that grew as Sir Ian's stock fell. Secondly, though the Green affair reeked, Sir Paul's behaviour in its aftermath—talking plainly, standing by his officers and starting an inquiry at once—earned the forgiveness of Boris Johnson, the Conservative mayor, and the gratitude of Jacqui Smith, the home secretary, whose department had ordered the investigation. Finally, Sir Paul was a continuity candidate around whom everyone could close ranks after a unpleasantly tumultuous spell. Both criticised for their actions during the Green affair, neither the mayor nor the home secretary stood to gain much from sacrificing Sir Paul so soon after his predecessor had been hounded from office.

The Met's new boss inherits a heaving in-tray. Keeping down street violence is the immediate priority. That, along with making police patrols more visible, may start to restore Londoners' faith in the force—especially important as the recession leads criminologists to predict rising crime rates. And on the horizon is the 2012 Olympics, for which security planning has fallen behind schedule.

Internal challenges also loom. One is winning over the rank and file, bruised by recent bad press (often deserved) on everything from the shooting of Jean-Charles de Menezes, mistaken for a terrorist, to a saga of racial discrimination claims by senior officers. Restoring confidence would have been easier for a "new broom" from another force; as part of the Met's existing establishment, Sir Paul will have to work hard to win people round.

That includes his political masters. Both the mayor and the home secretary back him at the moment, but many Conservatives see the Met itself as incorrigibly pro-Labour. This view began with Sir Ian and has been hardened by the Green affair and an extraordinary outburst by Bob Quick, a senior officer, who ranted about the "wholly corrupt" Tory machinery. A bad relationship creates the risk that a future Tory government might strip the Met of some of its national powers. Expect Sir Paul to launch a charm offensive against the mayor.

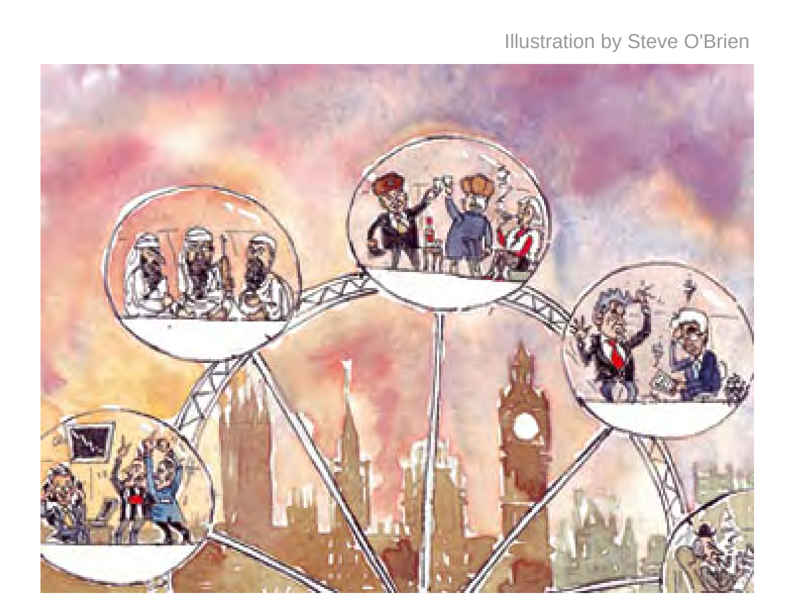
Bagehot

Reykjavik-on-Thames

Jan 29th 2009
From The Economist print edition

London's other names, and what they say about Britain's recent history

Illustration by Steve O'Brien



LONDON doesn't really have a nickname. At least, it doesn't have one that has stuck in the way that, say, the "Big Apple" has to New York, the "City of Light" to Paris or the "Windy City" to Chicago. In the last decade, however, during New Labour's long supremacy, visitors have bestowed a series of sobriquets on it: epithets that have captured the world's shifting perceptions of London and Britain, and the city and country's own changing preoccupations. The sequence nicely encapsulates Britain's evolving place in a globalised world—and its doubtful future.

Begin in the late 1990s, when the London property market recovered from the recession that had struck earlier in the decade. In the docklands—bombed by the IRA in 1996—the skyscrapers that had once seemed unviable filled up. The new government cemented its pact with the City: skimpy regulation in return for the growing tax revenues that helped to fund Labour's social programmes. Rents and ambitions soared. London became known, among financiers and architects, as Manhattan-on-Thames.

Manhattan-on-Thames was briefly the capital of a brand new nation: Cool Britannia. This was, according to the marketing men, a dynamic, modern, relentlessly neophile country—a land of Britpop, attention-seeking art involving unmade beds, and meetings in Number 10 between edgy rock stars and the new, thrusting prime minister. History seemed to have ended; Britain was embracing the world; things could only get better. All that now seems to belong to a distant, prelapsarian, naive age.

The debacle of the Millennium Dome finished off Cool Britannia; the terrorist attacks in New York and Washington in 2001 inaugurated a more sombre era. Manhattan-on-Thames became Londonistan. The term may have been coined first by French anti-terrorist police—angry at the British authorities' alleged laxity towards Islamist extremists—but it was used more widely after September 11th. The controversial mosque in Finsbury Park was Londonistan's emblem. Fairly or otherwise, the Tube and bus bombings of July 7th 2005 seemed to confirm the worries the label implied: nervousness about Britain's permeable borders, neurosis about multiculturalism and, in consequence, angst about the limits and encroachments of state security.

Yet continuing prosperity partly salved the anxiety. London recovered. Foreigners kept arriving, largely from the countries newly admitted to the European Union. But others came too, among them an influx of flamboyant Russians, some of them keen to launder their money and reputations and attracted by London's reliable courts, supposedly safe banks and kind tax regime. They brought joy to upmarket estate

agents, private-school headmasters and the footballers whose salaries they inflated (they also, less benignly, brought intrigue and polonium). Londonistan gave way to another nickname: Londongrad.

Londongrad was a metropolis of lunatic house prices and multiplying restaurants, ornamented by rich foreigners and serviced by poor ones. For a few years it seemed to be the capital not only of Britain but perhaps of the world too: the epicentre of globalisation. For many businessmen and financiers it was a no-questions-asked utopia of perpetual growth, lavish bonuses and capital flows, and unlimited easy credit.

Until the credit dried up. Now, suddenly, jobs are evaporating, the pound is falling, banks may soon proceed from partial to full nationalisation. The politicians who boasted of their light-touch regulation denounce the “casino capitalism” they encouraged. And as the *New York Times* has noted, some economists and traders have begun to refer to London by an ominous moniker: Reykjavik-on-Thames. Like the Icelandic capital, London is home to a stricken financial industry that once underpinned the economy, and to banks whose liabilities dwarf national output. As in Iceland the banks’ collapse has catalysed a new recession and rising unemployment, and may well contribute to the fall of a prime minister—even if Gordon Brown’s defenestration is likely to be more decorous than that of his ousted Icelandic counterpart.

“Reykjavik-on-Thames” exaggerates Britain’s predicament—probably. But it captures the way in which, at the moment, the country looks to some to be as much a victim of globalisation as its champion and beneficiary.

Peering into the abyss

Manhattan-on-Thames; Londonistan; Londongrad; Reykjavik-on-Thames: how will London and Britain be seen in a few years? According to David Cameron, the leader of the Conservatives, London will—at least if he becomes prime minister—be the capital of a freshly responsible nation. The financial miscreants will have been carted out of the City on the “day of reckoning” he promises; the rest of the city and the country will live within their means and save for a rainy day. London will be a sort of Grantham-on-Thames (Grantham being the home town where Margaret Thatcher acquired her faith in thrifty self-sufficiency). In Mr Brown’s imagination, London will have been reborn as Rooseveltville, resplendent with new train links, Olympic stadiums, airport runways and other job-creating grand public projects.

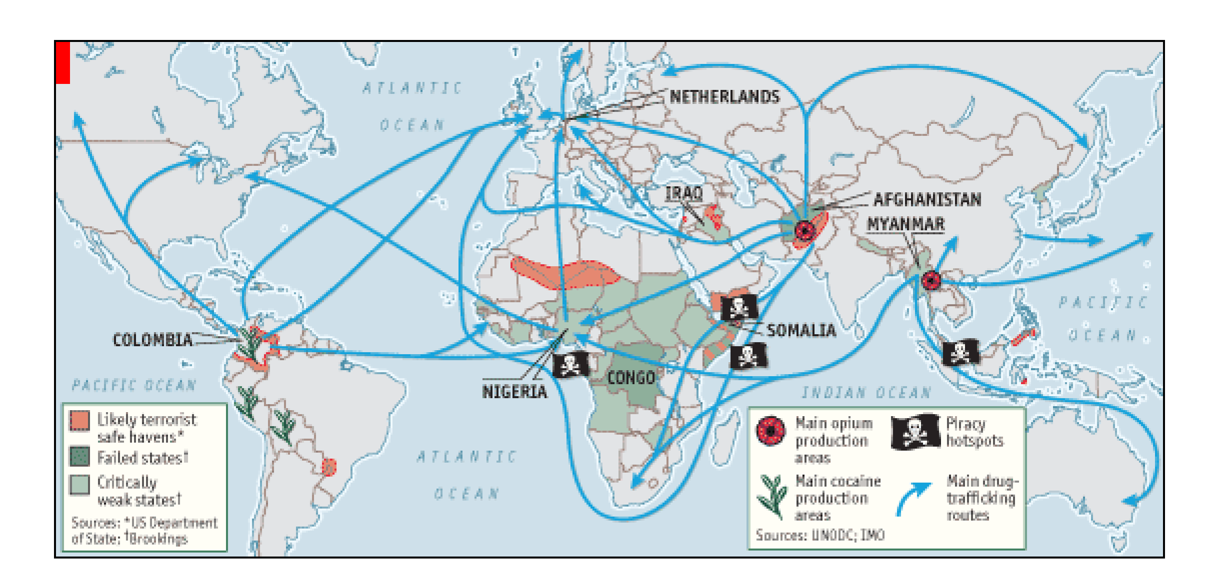
According to the most doom-laden predictions, meanwhile—in which the pound collapses utterly and the country goes bust—the city might look rather as it did in Victorian and Edwardian times, with legions of unemployed relying on sparse social services: London could revert to a somewhat more humane version of the “city of dreadful night”, “the empire of hunger” and “the abyss”, as it was known to sociologists a century ago. But it seems more likely that London will simply resemble the less prepossessing city it was in the 1970s and 1980s, before the excesses and excitements of the New Labour epoch: a drabber place, less magnetic to foreigners, worse hit than its rivals—like Britain as a whole—by the global downturn. London, in short, may revert to being plain old London-on-Thames.

Failed states

Fixing a broken world

Jan 29th 2009
From The Economist print edition

The planet's most wretched places are not always the most dangerous



IN ALMOST any discussion of world affairs, there is one thing on which doves and hawks invariably agree: much more needs to be done to shore up states that are failing, in a state of collapse, or so poor that they are heading in that direction.

For development-minded people, such benighted places are an obvious concern because of their desperate suffering; and for hard-nosed strategists, states that hardly work are places where terrorists could step into the vacuum. Indeed there is a certain convergence between these points of view: aid workers agree that security is essential to prosperity, and generals want economic development to boost security.

In America these days, defence planners say they worry more about weak states, even non-states, than about strong ones. "Ungoverned, undergoverned, misgoverned and contested areas" offer fertile grounds for terrorists and other nefarious groups, says the Pentagon's National Defence Strategy, issued last year. The penning of that document was overseen by the defence secretary, Robert Gates, who will remain in charge of defence policy under Barack Obama. Large chunks of its language could have been issued by bleeding-heart aid agencies or the United Nations: it speaks of the need to "build the capacity of fragile or vulnerable partners" and to address "local and regional conflicts" that exacerbate tensions and encourage drug-smuggling, gun-running and other illegality. To the chagrin of old-school sceptics, nation-building is now an integral part of American strategy.

Similarly, the European Union's declared security strategy sees state failure as an "alarming" phenomenon. It opines that: "Neighbours who are engaged in violent conflict, weak states where organised crime flourishes, dysfunctional societies or exploding population growth on its borders all pose problems for Europe."

A rather precise taxonomy is offered by Robert Cooper, a British diplomat and Eurocrat, in his book, "The Breaking of Nations". He splits the world into three zones: Hobbesian or "pre-modern" regions of chaos; areas ruled effectively by modern nation-states; and zones of "postmodern" co-operation where national sovereignty is being voluntarily dissolved, as in the European Union. In his view, chaos in critical parts of the world must be watched carefully. "It was not the well-organised Persian Empire that brought about the fall of Rome, but the barbarians," he writes.

Strategists have worried about failing states ever since the end of the cold war. At first, zones of war and

chaos were seen primarily as threats to the people living within them, or not far away. But since the attacks on America in September 2001 such places have increasingly been seen as a threat to the entire world. Western intervention is now justified in the name of fighting terrorism, not just of altruism.

Take the case of Somalia: America sent troops there in 1992 to help the United Nations stave off a humanitarian catastrophe, but the armed chaos of Mogadishu soon drove it out. In recent years, America has again been active in that region, carrying out air strikes in Somalia against suspected jihadist camps. It supported Ethiopia's military invasion in 2006 to defeat the Islamist militias that had taken power in Mogadishu (arguably causing even more chaos) and is now backing an African peacekeeping mission for the same reasons. The waters off the Somali coast, moreover, have become one of the prime zones of piracy at sea, disrupting shipping through the Suez Canal. Even China has felt the need to send warships to the Gulf of Aden to protect its shipping.

Afghanistan, too, is often seen as a classic example of the perils of collapsing states: acute poverty and years of civil war led to the rise of the Taliban and allowed al-Qaeda to turn into a global menace. After the American-led intervention in 2001, both have rebated themselves across the border in Pakistan's lawless tribal regions, from where they wage a growing insurgency in southern Afghanistan, destabilise Pakistan and plot attacks against Western targets around the world.

Western intelligence agencies say that, with the recent improvement in security in Iraq (a totalitarian state that became a failed state only after the American-led invasion), the world's jihadists now prefer to head for Pakistan, Somalia or Yemen.

Misrule, violence, corruption, forced migration, poverty, illiteracy and disease can all reinforce each other. Conflict may impoverish populations, increase the availability of weapons and debilitate rulers. Weak governments, in turn, are less able to stop corruption and the production and smuggling of arms and drugs, which may in turn help finance warlords, insurgents and terrorists.

AFP



Irregular forces, highly irregular wars: come to Taliban country

Instability breeds instability. The chronic weaknesses of civil institutions in Sierra Leone and Liberia contributed to the outbreak of devastating civil wars in both countries, fuelled by the profits from the illegal smuggling of “blood diamonds”. Meanwhile war and genocide in Rwanda contributed to the collapse of the Democratic Republic of Congo in the 1990s. The chaos there, sustained in part by fighting over mineral resources, sucked in Rwanda, Burundi and Uganda. Chad and Sudan support rebels in each other's countries.

At the very least, there is evidence that economic growth in countries next to failing states can be badly damaged. And if a poorly functioning but important oil-producing state like Nigeria were to fall apart, the economic fallout would be global. Moreover, weak governments may lack the wherewithal to identify and contain a pandemic that could spread globally.

That said, the interplay of these factors is hard to describe, and the very definition of failed states and ungoverned spaces is anything but simple. Few states have completely failed, except perhaps for Somalia. And even here, the territory is not completely ungoverned. A part of the country, called Somaliland, is more or less autonomous and stable—and another bit, Puntland, is relatively calm, although it is the source of much piracy. The region to the south is dominated by warring clans, but even here some aspects of normal life, such as mobile telephone networks, manage to survive.

Lesser breeds before the law

One starting point in any analysis of failed countries is the theory of Max Weber, the father of social science. He defined the state as the agency which successfully monopolises the legitimate use of force. But what does legitimate mean? In some places, state power is exercised, brutally but effectively, by whoever is top dog in a perpetual contest between kleptocrats or warlords whose behaviour is lawless in every sense.

If definitions are elusive, what about degrees of state failure? Perhaps the most detailed study is the index of state weakness in developing countries drawn up by the Brookings Institution, a think-tank in Washington, DC. This synthesises 20 different indicators and identifies three "failed" states—Somalia, Afghanistan and the Democratic Republic of Congo—along with 24 other "critically weak" ones. One striking feature of such tables is that states fail in different ways. Among the ten worst performers, Iraq is comparatively wealthy and does well in social welfare, but is highly insecure; Zimbabwe is comparatively secure, but ruined economically and politically. The next ten-worst performers are even more mixed.

The collapse of states is as varied as the states themselves. Some were never functioning states at all, just lines drawn on maps by colonisers. Many African borders encompassed lots of ethnic groups and divided some of them. When the colonialists left, so did the bureaucracies that supported these entities, abandoning them to poverty, civil war or both. The cold war helped fuel many conflicts, for instance in Angola and Mozambique, where superpowers backed rival factions. Other parts of Africa, such as Somalia, fell apart after the withdrawal of superpower support.

The conflicts of Central America died down in the years following the end of the cold war. But the fighting in Colombia has dragged on, as the FARC guerrillas finance themselves through drugs and kidnapping. The end of Soviet communism freed or created many countries in Europe. Some prospered as they were absorbed into NATO and the European Union, while others fragmented bloodily, notably Yugoslavia. Enclaves of "frozen conflicts" remain on Russia's periphery—for example Abkhazia, South Ossetia and Transdniestria which survive as unrecognised statelets with the Kremlin's support.

Whichever way state collapse is assessed, it will always be an imperfect measure of priorities for policymakers. On a map of the world using the Brookings index of weak states, the epicentre is self-evidently sub-Saharan Africa, particularly around Congo, with blobs of red in Iraq, Afghanistan and Myanmar. But this overlaps only in part with, say, the ungoverned spaces that America's State Department regards as the nastiest havens for international terrorists, such as al-Qaeda.

On that list, Iraq and Afghanistan figure prominently—but in these countries, arguably, the problem is more one of national insurgencies than international terror. Once the tribes of western Iraq (whose grievances were local) had been induced to switch sides to the Americans, al-Qaeda was quickly evicted from that area. Al-Qaeda's senior leaders are sheltering in Pakistan, yet this ranks as only the 33rd-weakest state on the Brookings index.

One area of concern is the Sahel, a vast semi-arid area south of the Sahara desert. The Americans fear that in this region Islamist terrorists could begin co-operating with existing rebel outfits, such as the Tuareg, or with drug smugglers. The Pentagon has created a new Africa Command to help monitor the area more closely and train local government forces.

The State Department identifies other ungoverned spaces such as Yemen (30th on the Brookings index), parts of Colombia (47th), the seas between the Philippines (58th) and Indonesia (77th), bits of Lebanon (93rd) and the "tri-border area" between Brazil, Argentina and Paraguay (none ranked as particularly weak).

Conversely many of the most wretched places in the world—Congo, Burundi, Zimbabwe, Haiti, Myanmar and North Korea—are not known as havens for international terrorists. Attacks linked to al-Qaeda, moreover, have been conducted in well-run countries such as Britain and Spain. For American counter-terrorism officials, the biggest terrorist threat to the homeland is posed by European radicals who are able to travel to America more freely than, say, a Yemeni. Some scholars worry about social breakdown in poor mega-cities. But to regard the British Midlands and the *banlieues* of Paris as ungoverned spaces would be stretching a point.

The common denominator for al-Qaeda's activity is not state failure, but the fact that attacks are carried

out by extremists claiming to act in the name of the world's Muslims. Their safe havens are not necessary geographical but social. Being based in a remote spot, far from government authorities, may be important for training, building *esprit de corps* and, in the view of intelligence agencies, trying to develop chemical and biological weapons.

But for al-Qaeda, remoteness alone is not enough. Terrorists need protection too, and that has to be secured from local populations as in Pakistan's tribal belt. International terrorists, moreover, need to be able to travel, communicate and transfer funds; they need to be within reach of functioning population centres. Stewart Patrick of the Council on Foreign Relations, an American think-tank, argues in a forthcoming book that international terrorists do not find the most failed states particularly attractive; they prefer "weak but moderately functional" states. The shell of state sovereignty protects them from outside intervention, but state weakness gives them space to operate autonomously.

Afghanistan's history is telling. Al-Qaeda was forged from the Arab volunteers who had fought with the Afghan *mujahideen* against the Soviet occupation of the country. With the end of the cold war and the fall of the communist government in Kabul, the country fell into civil war. Arab fighters largely pulled out in dismay.

Some went to Bosnia and Chechnya. Others intensified insurgencies back home in Egypt and Algeria. Osama bin Laden found shelter in Sudan under the protection of its Islamist regime. What took him back to Afghanistan was the rise of the Taliban. Afghanistan at that time was not an ungoverned space, but a state sponsor of terrorism; indeed, al-Qaeda arguably became a terrorist sponsor of a state.

Terrorism aside, what of other global plagues? Afghanistan is still the world's biggest source of the opium poppy, despite the presence of foreign troops. Next is Myanmar, also near the bottom of the pile. But Colombia, though not "critically" weak, is the biggest producer of cocaine. The cocaine routes pass through countries of all sorts; Mexico is among the top performers in the Brookings index, but is the main drugs highway to America. Similarly, piracy depends on geography. A non-existent state may allow pirates to flourish, but without the proximity of a shipping route they have no targets to prey on.

Measures of corruption, such as Transparency International's Corruption Perceptions Index, correlate strongly with the index of state weakness. But here too there are anomalies: Russia is ranked as a middling country in terms of state weakness, but does worse in the corruption index; Italy scores below some African countries.

When it comes to pandemics, there is no simple correlation between disease and dysfunctional states. The countries suffering most from HIV/AIDS are in southern Africa: apart from Zimbabwe, most governments in that region are quite well run. The states that have seen the most cases of the deadly H5N1 strain of bird flu are Indonesia, Vietnam, China and Egypt, none of them among the worst cases of misrule or non-rule.

Everybody agrees that more effective government around the world is desirable, especially for those living in or near broken countries. Failed states always cause misery, but only sometimes are they a global threat. Given that failures come in so many varieties, fixing them is bound to be more of an art than a science.

Catholics and Jews

A less than perfect touch

Jan 29th 2009
From The Economist print edition

It's not just the things Benedict does, but the way he does them

Reuters



WHATEVER history says about Pope Benedict XVI, it will not blame him for worrying too much about the feelings of people outside the global community of 1.1 billion or so people which he leads.

On January 24th, he lifted the excommunication of four traditionalist clerics who had been barred from the Catholic church in 1988 after being ordained as bishops by a rebel French ecclesiastic, Marcel Lefebvre. By itself, that might have been written off as an internal church matter—except that one of the four, Richard Williamson, a Briton, had denied the Nazi Holocaust, saying that "historical evidence is hugely against 6m Jews having been deliberately gassed."

A German pope already mistrusted by many Jews might have been expected to flinch at receiving such a figure just before the United Nations' Holocaust commemoration day—or, at least, to issue a statement deploring the Englishman's views. Not this pope. His spokesman said the ultra-conservative's comments were "totally extraneous" to the revoking of the excommunication. The Lefebvrists apologised to the pope "and all men of good will" over any offence caused, but not specifically to the Jews. Then, on January 28th, the pope himself expressed "full and unarguable solidarity" with the Jewish people.

That soothed tempers. Rabbi David Rosen, head of inter-religious affairs for the American Jewish Committee, called it "important, good and useful". But by then he and other senior Jews had been inveighing against the pope for four days.

It was the latest case of Benedict's seeming indifference to the impact and timing of his actions. Since his election four years ago, he has repeatedly ruffled feathers. In 2006 he enraged Muslims with a speech citing a medieval Islamophobe. The next year, he upset indigenous Latin Americans by saying that their evangelisation was not the "imposition of a foreign culture". Also in 2007, Benedict eased curbs on using the old Latin mass, stirring the first of several Catholic-Jewish rows. The Tridentine rite includes an Easter prayer for the conversion of Jews that has been amended but never dropped.

For Marco Ventura, a professor of law and religion at Siena University, the pope's abrasive style seems to reflect both conviction and a sense that tough talk plays well in the "religious market". On top of that, he says, Benedict probably just takes "a pride in being contrary".

In any case, the Vatican was not the only world authority under fire this week for giving heart to anti-Semites. A deputy foreign minister of South Africa, Fatima Hajaig, prompted horror among Jews in her country, and around the world, when she asserted at a pro-Palestinian rally that "control of America, just like the control of most Western countries, is in the hands of Jewish money". Wendy Kahn, director of South Africa's Jewish Board of Deputies, said the minister had "crossed all limits" by engaging in "anti-Semitism of the oldest and most classical kind".

Human capital and the crisis

Swinging the axe

Jan 29th 2009 | DAVOS
From The Economist print edition

Job-cutting has begun in earnest. But will the axe be wielded wisely?

Illustration by Claudio Munoz



THE headlines screamed that January 26th was “Black Monday” for jobs, after firms such as Caterpillar, Corus, Home Depot, ING, Pfizer and Sprint Nextel announced cuts of several thousand jobs each, due mostly to the rapidly deteriorating global economy. Alas, the consensus among the corporate bigwigs gathered this week at the World Economic Forum in Davos was that this marked only the beginning of the axe-swinging, and that there are blacker days to come.

This proved to be one of the big points of difference between the company bosses and the politicians brainstorming in the mountains. The politicians are primarily concerned with restoring demand enough to reverse the rising trend in unemployment; for many of the corporate leaders, ensuring the survival of their firms takes precedence over saving jobs. The difficult decision they face is not whether to cut, but how to do so in a way that strengthens their competitive position in the medium term rather than seriously damaging it.

The gloomy mood among bosses in Davos makes the worst-case scenario outlined in a new forecast from the International Labour Organisation (ILO) seem the most plausible of its possible outcomes. This supposes that if every economy in the developed world performs as it did in its worst year for unemployment since 1991, and every other economy performs half as badly as in its worst year, then the global jobless rate will rise to 7.1% this year—some 230m people, up from 179m in 2007.

The ILO’s most optimistic prediction is that global unemployment will rise only to 6.1% (from 6% in 2008). But that assumes that the world economy performs as the IMF forecast in November: global GDP growth of 2.2% in 2009, with a slight recession in the developed economies. The IMF has since become much glummer: this week it forecast growth of just 0.5%.

Already, firms are starting to find that their first round of cuts after the onset of the crisis is not enough. Caterpillar’s latest cut of 5,000 jobs is in addition to 15,000 already announced. Such is the frenzy of cutting that Challenger, Gray & Christmas, a recruitment firm that tracks employment trends in America, sought a crumb of comfort in its finding that over 50% of firms have cut jobs: it proclaimed in its latest report that “nearly half of employers avoid lay-offs.” But it pointed out that things would be even worse without the various innovative schemes adopted by companies to reduce labour costs without shedding

jobs. These include salary cuts, reduced hours and “forced vacations”.

As Challenger suggests, this seems in keeping with the suggestion by Barack Obama in his inauguration speech that people should “cut their hours [rather] than see a friend lose a job.” Already, by way of example, White House staff earning $100,000 or more have had their salaries frozen. Companies including Avis, Starbucks and Yahoo! have announced pay freezes for 2009.

Yet these creative job-saving schemes are unlikely to go anywhere near as far as Mr Obama would like. They may appeal as a way to buy some time as companies try to get a clearer picture of where the economy is heading, or to retain talented workers who are likely to be needed in the future, if not now. But they have little appeal once a firm has decided that it needs to scale back its operations. As the boss of a big American retailer put it privately at Davos, “We have to decide who we want on the bus and to motivate them as much as possible.” Clever ways to share the pain can demotivate everyone, especially if they are seen as merely postponing the inevitable job cuts, making everyone fearful.

Painful choices

Equally candidly, many bosses admit that the crisis is giving them a chance to restructure their firms in ways that they should have done before, but found a hard sell when things were going well. As a rule of thumb, a careful cull of the 10% of lowest performers can make a firm leaner by removing fat without damaging muscle. It is going beyond the 10%, as many firms are now starting to do, that poses the real risks to a firm’s competitiveness.

During the relatively modest downturn at the start of this decade, for example, many professional-services firms cut too deeply, especially in their lower ranks, and found they were poorly positioned when strong growth resumed sooner than expected, says Heidi Gardner of Harvard Business School. Firms built on pyramid structures in which senior managers mentored larger numbers of employees below them suddenly found that, in a growing economy, they lacked the mentors needed to manage the army of new recruits. Instead, they had to re-hire ex-staffers at higher salaries and, in some cases, abandon proven policies of hiring senior managers only from within, says Ms Gardner, who worked for McKinsey at the time.

This crisis is revealing how few firms have really thought through their talent strategies, says Mark Spelman of Accenture. Claims that “our workers are our most valuable assets” are too often platitudes, the emptiness of which is now being revealed. But those firms that have thought seriously about their talent needs have the opportunity to get ahead of those that haven’t, says Mr Spelman, not just by shedding poor performers but also hiring scarce talent from outside, in what is now a buyer’s market. Other tips from Mr Spelman include avoiding voluntary redundancy programmes, which encourage the most employable people to quit, and not firing the newest recruits on a crude “last in, first out” basis, as this cuts off the supply of future talent. Instead, firms should identify which workers they need to keep, and do what they must to retain them.

Governments can play a useful role or a harmful one, depending upon their attitude to companies, says David Arkless of Manpower, an employment-services firm. If they focus on working with firms to smooth the movement of labour to where the future work will be, for example by providing skills training and financial incentives to workers in transition, then the economic downturn could be less painful than now seems likely. (A quick recovery in lending to small businesses, the main drivers of job creation in most countries, would also help.) But if governments try to prevent firms from making the changes to their workforces that they want, the result is likely to be prolonged gloom.

Although Mr Obama’s support for strengthening the ability of unions to enter workplaces is arguably a worrying sign, the American economy is far more accommodating of flexibility in employment than many European countries. Mr Arkless, for one, says that without a dramatic change of attitudes to job-cutting in Europe, “there is no doubt that American firms will come out of this downturn better than anywhere else in the world, due to their flexible employment model.” This will provide no comfort to anyone facing the prospect of unemployment, but it is a message that politicians would do well to take to heart.

Pharmaceuticals

Buying time

Jan 29th 2009 | NEW YORK
From The Economist print edition

Will swallowing Wyeth cure Pfizer?

WHEN Jeffrey Kindler took over as the chairman of Pfizer two years ago, many looked forward to a new era at the American pharmaceutical giant. Unlike the firm's previous bosses, typically selected from the ranks of its technocrats, Mr Kindler was an amiable outsider and a lawyer. Investors hoped that instead of gobbling up rivals in an endless quest for scale, Mr Kindler would instead slim down the company in preparation for the dramatic drop-off in revenue at the edge of a patent "cliff" it is fast approaching. Lipitor, a cholesterol drug that earned Pfizer about $12 billion last year, loses patent protection in America in 2011; by 2013 products accounting for 38% of current sales will be exposed to price competition from generics.

But it seems that Pfizer has tamed the outsider, rather than the other way round. On January 26th Mr Kindler declared that his firm was making one of the industry's biggest acquisitions ever, buying Wyeth, a middling American rival, for some $68 billion. The deal is to be financed with a mix of cash, shares and short-term bank debt.

Financial markets' reaction was not kind. Pfizer's share price fell by roughly a tenth on the news, though it later recovered a bit. Moody's and Standard & Poor's, two credit-rating agencies, put the firm on their watch lists for potential downgrades. Mr Kindler did not help his case by saying that financing the purchase would mean a big cut in the firm's dividend, or by using the deal to bury news of a stunning $2.3 billion charge arising from settlement of a legal investigation into the allegedly improper marketing of a pain reliever.

So why did Mr Kindler take the plunge? One reason, he said, was that he could squeeze out some $4 billion in cost savings from the two firms. Claimed synergies have rarely materialised in past pharmaceutical deals, but this time Pfizer seems to mean business: it plans to shed nearly 20,000 jobs. Another attraction of the deal, Mr Kindler argued, is the chance to fill Pfizer's flagging distribution channels and weak research pipelines with fresh products. Wyeth sells consumer and animal-health products, which could help diversify Pfizer's revenue base (though it also suggests that Pfizer erred in selling its well-regarded consumer-products division to Johnson & Johnson, an American rival, two years ago).

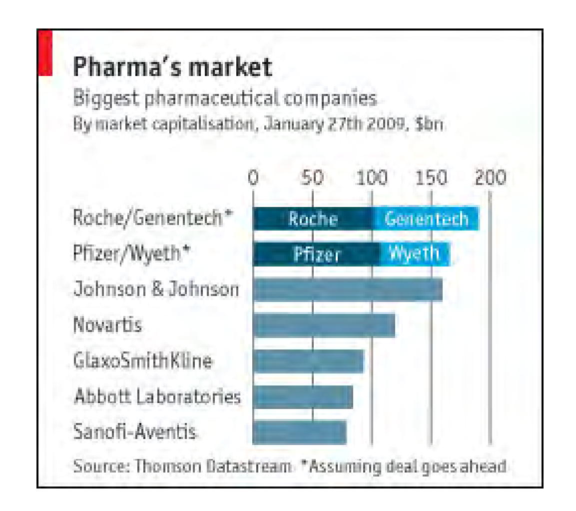
This deal is a useful "half step" forward for Pfizer, says Charles Farkas of Bain, a consultancy, but no more. He thinks Wyeth's assets will buy it some time but will not be enough to replenish the research pipeline or to replace Lipitor—not least because Wyeth faces its own patent cliff. Adding Wyeth's products to its mix would, by one estimate, reduce the share of Pfizer's sales exposed to generic competition in 2013 by just a few percentage points.

And that assumes that the deal will work. History provides one reason for scepticism. Michael Rainey of Accenture, a consultancy, who has scrutinised big deals in the industry, reached the damning conclusion that "nine out of ten deals created no value or negative value." Asked recently about mega-mergers, David Brennan, boss of Britain's AstraZeneca, scoffed that if big efficiency improvements were really possible, good managers would do them anyway, rather than pursuing mergers.

What about economies of scale in research? In fact there seems to be no connection between size and success. If anything, larding on extra layers of research managers stifles the entrepreneurial spirit that makes nimble biotechnology firms successful. That points to another potential weakness of the deal. Although Pfizer will gain access to novel vaccines and biotechnology, those innovative bits will come wrapped in big-company bureaucracy.

The final reason for concern arises from the vagaries of the financial crisis. Pfizer has obtained some $22.5 billion in bridge

financing for this deal from five banks. If its credit rating drops sharply, the banks have the right to revoke the loan—and Wyeth could walk off with a $4.5 billion break-up fee. That is unlikely given Pfizer's financial strength and solid credit rating, says John Moore of 3i, a private-equity firm.



But what will happen to the deal's financing if politics enters the fray is less clear. The American banks helping to finance the deal have benefited handsomely from taxpayer bail-outs. What will Mr Kindler say if he is hauled down to Washington, DC, to explain to Congress why he is using billions of dollars borrowed from such banks to implement a deal that, as he insisted this week, will result in the swift sacking of thousands?

Technology stimulus plans

Paved with good intentions

Jan 29th 2009
From The Economist print edition

Is "broadband for all" a recipe for recovery, or a boondoggle?

BEGGING for government help would have made you a pariah in most parts of the high-tech industry a few months ago. But these days state aid, and how to dole it out, are nearly as hotly debated in online hangouts as cloud computing or Steve Jobs's health. To understand the change of heart, just follow the money: the industry stands to do quite well from Barack Obama's $819 billion economic stimulus package. If America's new president has his way, a total of $37 billion will be spent on the digitisation of health records ($20 billion), a smarter power grid ($11 billion) and high-speed internet connections ($6 billion).

It is not just America that is betting on technology to help revive its economy. Though exact numbers remain to be determined, stimulus packages in other rich countries are likely to include large doses of technology spending, says Sacha Wunsch-Vincent, an economist at the OECD who has analysed more than two dozen such plans. A common theme is "broadband for all", echoed by a British government report called "Digital Britain" due to be published on January 29th.

Broadband, goes the thinking, could boost economies in much the same way as railways and highways did in previous eras. Research shows that it is a general-purpose technology with effects not just in the telecoms industry, but all over the economy, as it enables new business models, processes and services.

Several studies conclude that, in slack economies, more broadband means more jobs. The Brookings Institution, a think-tank in Washington, DC, projects that for every percentage point increase of broadband penetration at state level, employment increases by 0.2% to 0.3% per year, equivalent to 300,000 jobs nationally. In the European Union, greater availability of broadband internet connections could create more than 2m jobs by 2015, according to a study by Micus and WIK-Consult, two German consulting firms.

There is also evidence that investment in other sorts of information technology could boost growth. The Information Technology and Innovation Foundation, an American think-tank, estimates that $10 billion invested over a year in health-related technology, particularly standardised electronic health-records, would create more than 200,000 jobs. And spending $50 billion over five years to upgrade the power grid with technology such as "smart" electricity meters could mean nearly 240,000 new jobs a year, it says.

AP



Look! A job!

But even if these numbers are right, throwing state funds at technology may not be the best approach. Other things can be done to increase broadband penetration before dipping into the public coffers. A recent study for the British government by Francesco Caio, a former chief executive of Cable & Wireless, listed a few of them, including accelerating the release of radio spectrum, fostering competition and relaxing the rules that prevent companies from stringing up overhead cables.

Furthermore, there is no clear market failure that demands government intervention, argues Michael Nelson, a professor at Georgetown University. Indeed, although America ranks 15th among OECD countries in broadband penetration, the country's telecoms firms are already spending billions building next-generation networks. And simply digitising health records or promoting the spread of broadband may not produce the desired economic knock-on effects without investment in the fields that will use these technologies, such as health and education.

Many stimulus plans appear to be long on promoting broadband and short on saying how it would be used, says Mr Wunsch-Vincent. There are also many unanswered questions over how to dole out the money. Should the subsidies take the form of tax breaks or targeted grants? Should they go to existing telecoms operators or be directed towards new entrants? And should recipients be forced to open up subsidised networks to rivals?

Perhaps the biggest risk of all these broadband plans is that incumbents will exploit the crisis to gain regulatory concessions limiting competition and open access to their networks in exchange for promises to invest. This could even help recreate the telecoms monopolies of old. But if this recession has proved anything, it is that what goes around, comes around.

Siemens and Areva

Nuclear fission

Jan 29th 2009 | PARIS
From The Economist print edition

Franco-German industrial relations take a sharp turn for the worse

“THIS is not the way you behave in business—normally you send signals,” spluttered a French nuclear executive this week at the news that Siemens, Germany’s engineering giant, would divest the 34% stake it has held since 2001 in Areva NP, a Franco-German joint venture in nuclear reactors. Until this week Areva NP was an example of a successful partnership between French and German companies in a promising industry. Nuclear power is in the midst of a global comeback, and Areva NP’s new design, the European Pressurised Reactor (EPR), is leading the field against competing blueprints from American and Japanese rivals.

Being a minority shareholder, the German firm complained, “considerably limits the entrepreneurial manoeuverability of Siemens within the joint venture.” Siemens had been trying to increase its influence, either by lifting its stake in Areva NP to 50%, or by swapping its share of the joint venture for a slice of the company’s French parent, Areva. But the French government, which has a majority stake in Areva, blocked Siemens’s ambitions, probably because it wants to stay in control of a strategic industry. The German firm now intends to exercise a put option, meaning that Areva will have to stump up around €2 billion ($2.6 billion) to buy back the stake at some point over the next three years. There is a small chance that Siemens will get its way after all—its decision will not be final until Areva buys back its shares—but that is unlikely, says an insider.

Siemens will have agonised over the decision. Walking away from Areva NP means turning its back on a big chunk of its former assets. It became a shareholder in Areva NP not just by contributing money, but by bringing Germany’s entire nuclear-power industry to the venture. It could have chosen to develop its own nuclear business, but decided instead to seed a Franco-German partnership. The two companies are closely intertwined: Areva NP has about 3,600 German employees, and the engineering for its first EPR, now under construction at Olkiluoto in Finland, is based at one of Siemens’s production units near Nuremberg.

The Germans have long feared that the French government planned to squeeze them out of Areva, and may have decided to pre-empt such a move. Nicolas Sarkozy, the president of France, wants to create a national nuclear-energy champion, and Alstom, a French engineering company, has been lobbying hard for a merger with Areva. A decision on Areva’s future ownership is expected soon, and since Alstom would replicate what Siemens does, the German company was an obstacle. The sudden rupture probably also reflects poor relations between the French and German governments following Mr Sarkozy’s initiative to form a Mediterranean union which initially excluded Germany.

Nevertheless, the decision came as a shock to Areva. Until this week, says Nicolas Véron of Bruegel, a Brussels think-tank, Areva NP was the main counter-example to the general presumption that Franco-German industrial ventures do not work. “It would be a big blow to the bilateral relationship to see this one disappear too,” he says. At EADS, a Franco-German-Spanish aerospace group that is the parent of Airbus, relations have been strained, with the Germans often suspecting the French of trying to grab power. The deepest wound was inflicted five years ago when Aventis, a drugs company formed in 1999 by a merger between Germany’s Hoechst and Rhône-Poulenc, a smaller French firm, merged with Sanofi-Synthélabo, which was also French. The deal, strongly supported by Mr Sarkozy, then France’s finance minister, meant that the company became more French than German.

Siemens’s exit is bad news for Areva, too. Areva’s chief executive, Anne Lauvergeon, is fiercely opposed to a merger with Alstom, and the German firm’s retreat removes an important line of defence. Eventually Areva will face a new competitor as Siemens develops its nuclear capabilities, perhaps in partnership with Atomenergoprom, a Russian state-owned nuclear-energy firm with which it already has a relationship. For its part, Areva argues that it needs money all the more urgently now that it has to buy out Siemens’s stake and fund the development of the EPR on its own. “A merger with Alstom would not bring adequate financial resources,” says an Areva executive. Areva’s preferred option is to issue more shares on the

market, thus reducing the government's control.

For the time being Siemens and Areva will still be bound together in one way at least. Teollisuuden Voima (TVO), a Finnish utility, is demanding €2.4 billion in compensation from the two firms for delays in building the EPR at Olkiluoto, and they in turn are demanding €1 billion from TVO. The former partners will be seeing plenty of each other in court. Beyond that, however, it may be time for Areva to rename its reactor the "FPR".

Sweden's car industry

For sale

Jan 29th 2009
From The Economist print edition

Saab and Volvo are on the block. But are there any buyers?

THE Swedish car industry is up for sale. Saab and Volvo are on the block because their owners, General Motors (GM) and Ford respectively, can no longer afford to keep them. But there are important differences. GM may have only weeks to divest itself of Saab, whereas Ford is a slightly less desperate seller.

GM, which would have gone bust without the emergency federal loans it received at the end of the year, faces a deadline on February 17th. It must show progress towards viability or risk having to pay the taxpayer back at the end of March. Most attention will be focused on negotiations with unions and bondholders. But GM also wants to show that it is close to spinning off Saab as a separate entity, either to sell it or to let it sink or swim on its own. Ford, which continues to believe it can survive without a bail-out, is under less immediate pressure to dispose of Volvo, but would still love to find a buyer.

The differences between the two Swedish firms extend beyond those of their troubled owners. Not only is Saab much smaller—it sold 125,000 cars in 2007, compared with Volvo's 458,000—but it has been a much greater flop for GM than Volvo has for Ford. Speaking this month at the Detroit motor show, Bob Lutz, GM's vice-chairman, described Saab as a financial disaster that had made a profit just once in the 20 years that GM has owned it (GM bought 50% in December 1989 and the rest a decade later). Overall, owning Saab may have cost GM up to $5 billion, and GM loses as much as $5,000 on every Saab it sells in America.

The only reason GM kept the company so long, said Mr Lutz, was that it loved the marque and the cars. But in truth the relationship has never been happy. GM once saw Saab as a potential rival to BMW. But whereas BMWs became the default choice of striving young professionals in the 1990s, buying a Saab was a statement of eccentric individualism—something utterly alien to GM's corporate culture. GM constantly tried to force its often stodgily conventional engineering on Saab in an effort to save money, while Saab, just as stubbornly, attempted to preserve what was different about its cars, such as putting the ignition on the floor by the gearbox. Not surprisingly, the results pleased neither GM's beancounters nor Saab enthusiasts.

Saab's idiosyncratic way of doing things, and its powerful unions, make it unusually difficult to sell. It has a strong brand, but one that is neither truly premium nor, these days, sporting. It was once a pioneer of turbocharging, but its technology no longer stands out.

In December the centre-right Swedish government put together a bail-out package that would provide Saab, Volvo and their suppliers with up to $3.5 billion in loans and credit guarantees. But it is adamant that the money must be spent in Sweden. Joran Hagglund, state secretary in the ministry of enterprise, said this week that GM had yet to present him with a business plan that would unlock the funding.

Might, for example, production of Saab's biggest car, the new 9-5, scheduled to be built at Rüsselsheim in Germany, be shifted to under-employed Trollhattan in Sweden? GM insiders put the cost of the move at $200m on top of the $100m needed to prepare the car for launch at the end of the year. There is also talk within Saab of moving production of the 9-4x crossover, due for launch next year, from a GM plant in Mexico to Sweden. Work on the urgently needed successor to the ageing 9-3 has been put on ice. Saab's chief executive, Jan-Ake Jonsson, maintains that once the market returns to normal his company can be profitable, but his is a lonely voice.

Volvo, which Ford acquired in 1999 for a hefty $6.45 billion, has been a disappointment rather than a disaster. The company has been modestly profitable for much of the time Ford has owned it. But the losses have been mounting, especially in America because of the weak dollar. In 2007, when it had its best-ever global sales performance, Volvo still lost $164m. With sales for 2008 down 18%, the bottom line made grim reading when Ford announced its results on January 29th. Volvo's losses last year amounted to

nearly $1.5 billion, $736m of which fell in the final quarter.

But the deciding factor is that although Volvo and Ford use a lot of common technology, keeping Volvo does not fit with the “One Ford” strategy on which Ford’s boss, Alan Mulally, has staked his firm’s survival. He has already sold Aston Martin and Jaguar Land Rover. Volvo is another distraction Mr Mulally could do without.

Ford’s frustration with Volvo is that despite its many loyal customers, its well-earned reputation for safety and the occasional hit, such as the XC90 sport-utility vehicle, it has never quite been able to shake off its “sub-premium” image. Like Saab, Volvo sits uncomfortably between the volume producers and such marques as Audi, BMW and Mercedes.

Even so, it has more to offer a potential buyer than Saab. It is bigger, has a global dealer network and its sales are more evenly distributed between Europe, North America and emerging markets, particularly China and Russia, where it has done well. And the just-launched XC60 mid-sized crossover is proof that when it comes to safety and Scandinavian style, Volvo has lost none of its mojo.

Whether anyone will want to take Volvo off Ford’s hands is another matter. Most of the big European manufacturers have had a look and decided to pass. Despite persistent rumours of interest from several Chinese firms, a bidder has yet to emerge. Stephen Odell, recently appointed as the first non-Swede to run Volvo, insists that the only thing on his mind is returning the firm to profitability. But Mr Mulally must be hoping that a buyer turns up long before that distant day arrives.

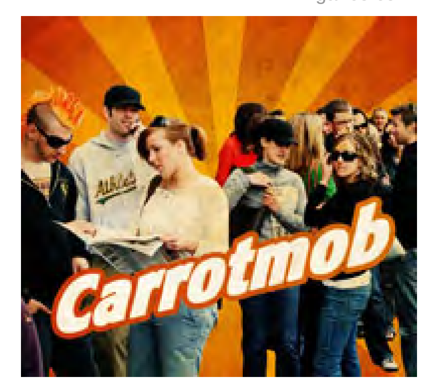
For-profit activism

Change we can profit from

Jan 29th 2009 | SAN FRANCISCO
From The Economist print edition

A start-up inspired by Barack Obama

virgance.com



Shopping for a good cause

RESIDENTS of San Francisco have been signing up enthusiastically for a new green-energy campaign called 1BOG. Short for "one block off the grid", it aims to convince homeowners to switch to solar energy one block at a time, by organising them into buying clubs. Members get a discount on solar panels, and typically try to get their neighbours to sign up too. The city has also seen several recent examples of Carrotmobs—crowds of activists who buy everything in the winning shop in a contest between retailers to be the greenest.

What makes these two examples of activism stand apart is the driving force behind them: the campaigns are owned by Virgance, a start-up based in San Francisco's trendy South Park district that was founded by Brent Schulkin, a self-described "road warrior turned activist", and Steve Newcomb, a Silicon Valley serial entrepreneur. Having sold his previous firm, a search engine called Powerset, to Microsoft, Mr Newcomb says he wanted to do more than just start another technology company; he wanted to do well by doing good. "I started looking at activism as a potential start-up industry," he says.

In classic Silicon Valley fashion, the firm takes its name from a plot device in "Star Wars". The inspiration for its business model is Electronic Arts, a video-games firm that releases "many games a year, and hopes a couple are hits." For games, read campaigns. Just as Electronic Arts has built a distribution platform to support its games, Virgance's role is to find campaigns that it can help to succeed through a four-pronged support strategy that Mr Newcomb says draws heavily on the way in which Barack Obama motivated and managed his activists. This includes a volunteer network ("boots on the ground"), an "activism presence in Facebook", a team of paid bloggers who promote Virgance campaigns, and YouTube videos supporting its causes.

The revenue model varies according to the nature of the campaign. Carrotmob is suitable for paid sponsorship by firms that want cause-related branding. 1BOG gives Virgance a slice of the discount it negotiates from clean-tech providers. Another campaign, Lend Me Some Sugar, is based on a Facebook application that gives users virtual sugar cubes for donation to a cause of their choosing. A sponsoring firm then turns sugar cubes into dollars from its corporate social responsibility budget; Virgance is paid to organise the process. A fourth idea is to set up a green venture fund on Facebook, in which users will be invited to invest as little as $100. Virgance will take a cut of any investment profits.

Mr Newcomb says being a for-profit company enables it to grow faster and achieve more social impact than a non-profit, because it can afford to pay its employees competitive salaries and can raise capital from investors, rather than relying on donations. It is part of a trend: other for-profit do-gooders include Bono's (RED) brand, which raises money for the Global Fund on Tuberculosis, AIDS and Malaria, and the Facebook Causes application, which makes it easier for people to donate to their favourite charities. Watch this space.

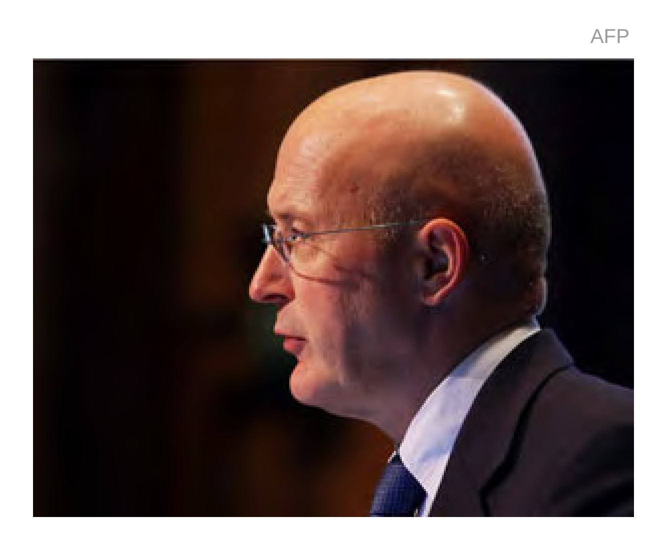
Face value

Casino Royal

Jan 29th 2009
From The Economist print edition

As chairman of Royal Bank of Scotland, Sir Philip Hampton is in his hottest seat yet

AFP



SIR PHILIP HAMPTON began his career as an accountant "for reasons", he says, "that still elude me." He has since specialised in trying to drag big, venerable British companies out of the doldrums. Over the years he has been finance director of British Steel, British Gas, British Telecom and Lloyds TSB, and, since 2004, chairman of J. Sainsbury, a supermarket group. Yet even by those standards his latest post, as chairman of Royal Bank of Scotland (RBS), is daunting. RBS is huge rather than just big: it was the world's largest bank by assets at the end of 2007. By corporate standards it is ancient rather than merely venerable, having been founded in 1727 and predating Robert Burns and even, some say, the kilt. And to say RBS is in the doldrums would be a gross understatement. It is on life support, 70% state-owned after receiving two bail-out packages in the past four months. On January 19th it signalled that it had made a loss of as much as £28 billion ($52 billion) in 2008, the biggest in British business history.

There is something of the vicar about Sir Philip: he has a measured, analytical mind and expresses himself softly and politely. It would be hard to find a bigger contrast with the gung-ho, monosyllabic culture that turned RBS into an acquisition machine. It swallowed up NatWest in Britain, Charter One in America and eventually led the consortium that bought ABN AMRO in 2007. That deal has come to symbolise the excesses of the banking bubble: two of the three consortium members, RBS and Fortis, have since been taken into majority state control. Sometimes, Sir Philip notes, "You need acquisitions like a hole in the head."

His manner is calm, but he has seen plenty of service fighting scary financial fires. When Sir Philip joined British Telecom (now BT) in 2000, net debt had soared to almost £30 billion, much of it funded by short-term commercial paper—a situation that might have led to bankruptcy in today's credit markets. The medicine included a giant debt-refinancing package and what was at the time the largest rights issue in British history (RBS now holds this title, after raising £12 billion in equity in early 2008). "If you're not totally honest about your financial position, you unfortunately get in a pickle," he says. His arrival at RBS in April is likely to herald another brutal re-examination of its books for bad debts.

Sir Philip says his management style is "consensual". He is not an operations man and has never been, or wanted to be, a chief executive. At J. Sainsbury, where he has a close working relationship with Justin King, that division of labour has worked well. Sir Philip says he "gets on well" with Stephen Hester, the new chief executive of RBS, who was appointed late last year, and that "we've known each other a long time." Still, it seems likely there will be a further cull of RBS's top brass and board. People are "nearly always behind financial problems," he says. At J. Sainsbury his appointment was followed by a clean-up of senior executives and directors. This lack of sentimentality applies even to himself: at Lloyds he was

ousted in under two years, having resisted the bank's strategy of maintaining a high dividend and a policy of growth at the expense of bolstering its capital position.

The key to managing crises, he says, is to "keep an eye on the long term while you're dancing in the flames." The long-term question for RBS is how far its empire will be pared back. It has already sold its minority stake in Bank of China, and with only one-third of its risk-weighted assets residing in its core British business there are lots of opportunities for disposals and spin-offs (its American unit being a prime candidate). Although he has presided over a period of growth and investment at J. Sainsbury, Sir Philip has also helped dismantle several business empires. He was intimately involved in the break-up of British Gas (now BG) into three separately listed companies and British Telecom's decision to spin off its mobile arm, O2. Private shareholders should not be too worried by this. O2 was eventually bought for a large premium by Spain's Telefónica, and the break-up of the gas monopoly helped unleash BG Group, now a much-admired global leader in the upstream energy market.

Leaning on the state—at arm's length

That assumes, of course, that RBS still has some private shareholders. With pro-forma assets of £1.7 trillion, more big losses are likely, but with a market capitalisation of just £6 billion, further equity injections from the government would probably leave the bank entirely state-owned. Sir Philip says "everyone is working hard to avoid full nationalisation, though it can't be ruled out," and that the government's proposed insurance scheme, under which the state will guarantee the bad assets on banks' balance sheets, will be "pivotal". If it is big enough, and the terms are attractive, it could be an alternative to further capital injections.

Sir Philip is used to refereeing disagreements between groups of shareholders. In 2007 J. Sainsbury faced an ultimately abortive bid from a Qatar-backed buy-out fund, which many private shareholders supported but which the Sainsbury family was less enthusiastic about. Still, it will be difficult dealing with both private investors and a government desperate to preserve jobs and boost lending in the face of a deep recession. The RBS stake will be held through UK Financial Investments, a new state holding company, which Sir Philip briefly chaired before accepting the job at RBS. During his short tenure he insisted that he would resist political interference in banks' operating decisions; he must now hope that his successor will be just as robust.

Within the dog's breakfast of RBS there is a still-strong business with strong brands. Isolating and reviving it will be hard enough. Doing so while also trying to secure government help, but avoid full state ownership, will be even more difficult. Sir Philip is a keen sailor and has crossed the Atlantic in his yacht, but it may be many years before he manages another big trip. At least RBS now has someone at the helm whose ambition is not to rule the world, merely to circumnavigate it.



Correction: Car industry

Jan 29th 2009
From The Economist print edition

In our briefing on the global car industry ("The big chill", January 17th 2009) we reported that Rolls-Royce sold no vehicles in America in December 2008. Rolls-Royce has since told *The Economist* it sold "more than 70 cars", and Autodata, a market-research firm, says Rolls-Royce sold 31 cars that month.

Asian economies

Troubled tigers

Jan 29th 2009 | HONG KONG
From The Economist print edition

Asia needs a new engine of growth



IT SEEMS so unfair. Most Asian economies have been models of prudence. While American and European households were borrowing up to the hilt, Asian ones were tucking away their savings. While rich-country banks were piling into ever-riskier assets, Asian banks kept their holdings of such assets small. And while America and Britain were sucking up the world's savings, Asian governments piled up vast stocks of foreign reserves.

Yet many of Asia's tiger economies seem to have been hit harder than their spendthrift Western counterparts. In the fourth quarter of 2008, GDP probably fell by an average annualised rate of around 15% in Hong Kong, Singapore, South Korea and Taiwan; their exports slumped more than 50% at an annualised rate. Share prices in emerging Asia have plunged by almost as much as during the Asian financial crisis a decade ago. That crisis was caused by Asia's excessive dependence on foreign capital. This time the tigers have been tripped up by their excessive dependence on exports.

Asia's emerging economies have long been the world's most dynamic, with GDP growing at an annual rate of 7.5% over the past decade, two and a half times as fast as the rest of the world. Only last summer, many of these countries were being warned by foreigners that they were growing too fast and needed to raise interest rates to prevent a surge in inflation. Now, many seem to be in free fall and the news is likely to get grimmer.

In the fourth quarter of 2008, real GDP fell by an annualised rate of 21% in South Korea and 17% in Singapore, leaving output in both countries 3-4% lower than a year earlier. Singapore's government has admitted the economy may contract by as much as 5% this year, its deepest recession since independence in 1965. In comparison, China's growth of 6.8% in the year to the fourth quarter sounds robust, but seasonally adjusted estimates suggest output stagnated during the last three months.

Asia's richer giant, Japan, has yet to report its GDP figures, but exports fell by 35% in the 12 months to December. In the same period, Taiwan's dropped by 42% and industrial production was down by a stunning 32%, worse than the biggest annual fall in America during the Depression.

Asia's export-driven economies had benefited more than any other region from America's consumer boom, so its manufacturers were bound to be hit hard by the sudden downward lurch. Asian exports are volatile anyway (see chart 1). And though the 13% fall in the region's exports in the 12 months to December was slightly smaller than in 1998 or 2001, those dismal records seem certain to be beaten soon.

The plunge in exports has been exacerbated by the global credit crunch, which made it harder to get trade finance. Destocking on a huge scale has further slashed output. Trade within Asia has dropped by even more than the region's sales to America or Europe. Exports to China from the rest of Asia were 27% lower in December than a year earlier, partly reflecting weaker demand for components for assembly into goods for re-export.

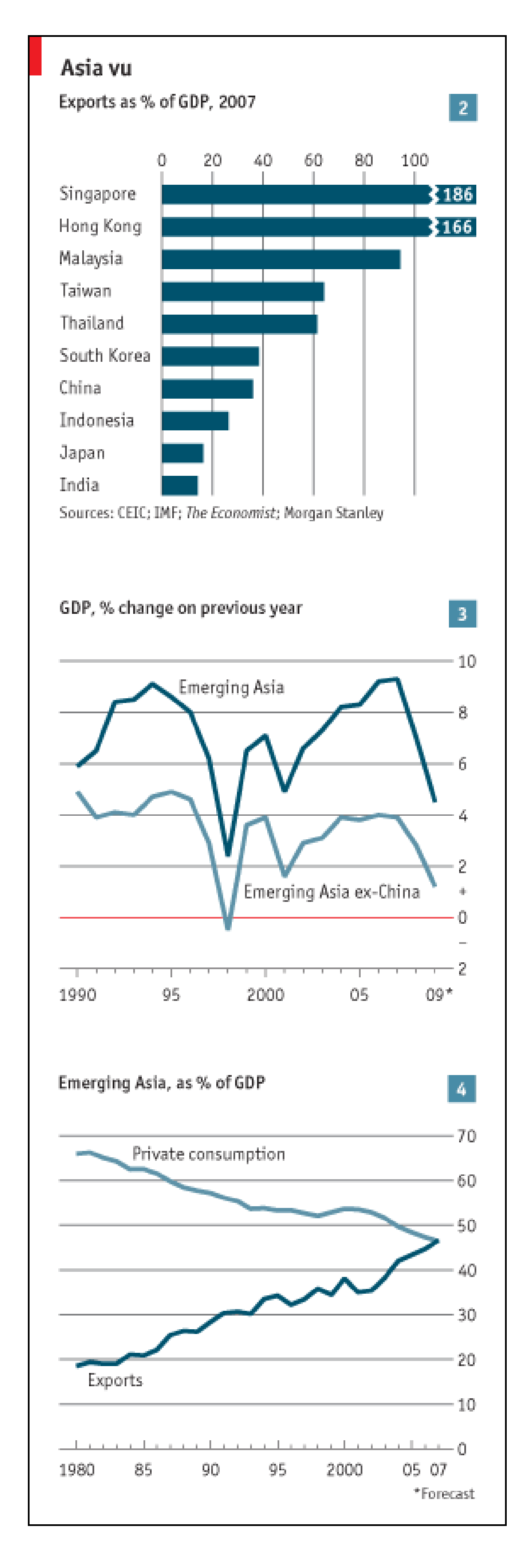
Shocking as the export figures are, they are not entirely to blame for Asia's woes. A closer look at the numbers reveals that in most countries imports have fallen by even more than exports, and that weaker domestic demand explains a larger part of the slump.

In China, for example, weaker domestic spending—mainly the result of a collapse in housing construction—accounted for more than half of the country's slowdown in 2008. In South Korea, net exports actually made a positive contribution to GDP growth in the fourth quarter, while consumer spending and fixed investment fell at annualised rates of 18% and 31% respectively. South Korea is an exception to the rule of Asian prudence. Its households' debt amounts to 150% of disposable income, even higher than in America. The banking system, which borrowed heavily abroad to finance a surge in domestic lending has also been badly hit by the global credit crunch, making it harder for firms to finance investment.

Domestic spending has collapsed elsewhere. Over the past 12 months, retail sales have fallen by 11% in Taiwan, 6% in Singapore and 3% in Hong Kong. As big financial centres, the two city-states have been battered by the global storm. Both have high levels of share ownership, so tumbling stockmarkets and property prices are depressing consumption. In Hong Kong average house prices have already fallen by almost 20% since the summer and Goldman Sachs, an investment bank, forecasts another 30% drop by the middle of 2010.

A recent report by Frederic Neumann and Robert Prior-Wandesforde, two economists at HSBC, a large bank, argues that Asia is suffering two recessions: a domestic one as well as an external one. Domestic demand had been expected to cushion the blow of weaker exports, but instead it was hit by two forces. First, the surge in food and energy prices in the first half of 2008 squeezed companies' profits and consumers' purchasing power. Food and energy account for a larger portion of household budgets in Asia than in most other regions. Second, in several countries, including China, South Korea and Taiwan, tighter monetary policy intended to curb inflation choked domestic spending further. With hindsight, it appears that China's credit restrictions to cool its property sector worked rather too well.

The two recessions reinforced one another. Part of the slump in domestic spending is attributable to falling exports, which force firms to cut investment and lay off workers. This makes it hard to say whether domestic or external demand is more to blame for Asia's distress. The importance of exports to the Asian miracle has long been controversial anyway. The crude figures show that, on average, emerging Asia's exports amount to 47% of their GDP, up from 37% ten years ago. The share varies from 14% in India to 186% in Singapore (see chart 2). In Japan, which is often viewed as an export-driven economy, exports are only 16% of GDP.



But this ratio overstates a country's dependence on external demand if exports have a high import content. China's exports account for 36% of GDP, but about half of them are "processing exports", which contain a lot of imported components. Thus the impact on GDP growth of a fall in exports is partially offset if imports fall too. Estimates suggest that domestic value-added from Chinese exports is a more modest 18% of GDP.

An alternative measure of the importance of exports is the change in net exports in real terms. Between 2002 and 2007 the increase in net exports contributed only 15% of real GDP growth in China. In contrast, net exports accounted for half of all growth in Singapore and Taiwan. This measure understates the total impact, though, because it ignores the spillover effects of exports on business confidence, investment,

employment and consumer spending. Either way, the smaller economies, Hong Kong, Singapore and Taiwan, are heavily export-dependent; the giants, China and India, less so.

Asia's recoveries from previous downturns have been led by a rebound in exports to the rich world. This is unlikely in the near future. The question is, might domestic demand now take up some of the slack? There are reasons to think so. Falling commodity prices are boosting consumers' purchasing power, just as they squeezed it last year. More important is the impact of monetary and fiscal expansion.

With the exceptions of South Korea and India, Asia has so far been spared the financial dislocations that are plaguing the West. The HSBC economists reckon that the region is more likely to suffer a credit pinch than a full-scale crunch. In contrast to America and Europe, where excessive debt could depress spending for years, most Asian households and firms (except in South Korea) have modest debts. And, because of healthier banking systems, Asian banks are less likely than Western ones to react to the crisis by refusing to lend. Hence interest-rate cuts and the easing of credit controls should be more potent than elsewhere. No less important is Asia's massive fiscal pump-priming. This is also likely to be more effective than elsewhere because the private sector is in better shape and able to respond by spending more.

Asia has never before deployed its monetary and fiscal weapons with such force. Every country across the region has cut interest rates and announced a fiscal stimulus. In previous downturns, Asian governments were often constrained by dire public finances or the need to support currencies. But most countries entered this downturn with small budget deficits or even surpluses. All the main Asian emerging economies apart from India have relatively low ratios of public debt to GDP.

Though the true size of the fiscal stimulus in some countries, notably China, is probably less than the headline-grabbing figures suggest, they are still impressive. After correcting for double counting and unrealistic measures, China, Singapore, South Korea and Taiwan will all enjoy a fiscal stimulus of at least 3% of GDP in 2009. China has signalled that more measures may follow over the next couple of months; it can certainly afford to spend more. On January 22nd, Singapore's government announced a package of measures equivalent to 8% of GDP. For the first time, this will be financed partly by dipping into the government's vast reserves.

The effectiveness of fiscal easing depends on its composition as well as its size. Income-tax cuts planned in South Korea and Taiwan will have only a modest impact if the money is saved not spent. Corporate tax cuts, planned in Singapore, may not spur investment when profits are plunging. Taiwan's government is attempting to boost consumer spending by issuing shopping vouchers worth NT$3,600 ($107) per person. Economists are sceptical about whether this will produce new spending, but the scheme is being watched closely by other Asian governments.

More promising is the fact that every country is planning to boost infrastructure spending. In the short term, this is probably the best way for governments to boost spending and jobs; in the longer term better roads and railways should boost productivity. Fiscal tightening in emerging Asia after the 1998 crisis caused governments to reduce capital spending; as a result, public infrastructure in some countries, notably Indonesia and Thailand, is probably worse than a decade ago. So there is plenty of room to spend more.

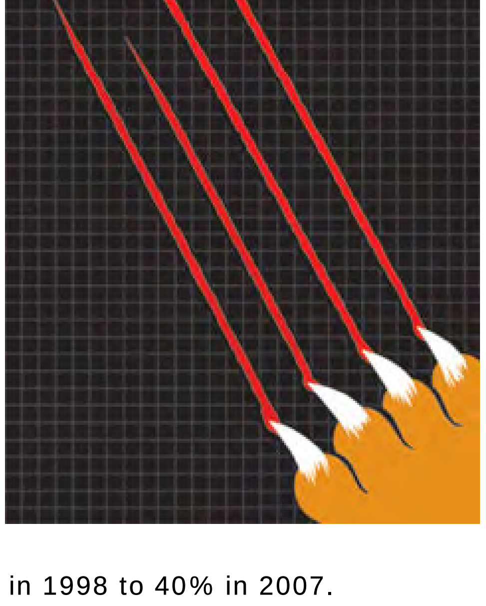
If (still a big if) China and others fully implement their stimulus plans, domestic demand could start to recover in the second half of this year even if exports remain weak. Average growth in emerging Asia might fall to only 4-5% in 2009 as a whole, half its pace in 2007 and the slowest rate since the Asian financial crisis. But it would be well above the trough of 2.4% in 1998 (see chart 3). That average conceals a wide variation. The economies of Hong Kong, Singapore, South Korea and Taiwan will all contract this year, while the bigger, but less open economies of China, India and Indonesia should hold up better.

Shop or drop

However, Asian governments have more than this year's growth rate to worry about. Beyond the immediate crisis, where will growth come from? America's consumer boom and widening trade deficit, which powered much of Asia's growth over the past decade, has come to an end. America's return to thrift is unlikely to prove a cyclical blip. For years to come, Americans will have to save more and import less. Asia's export-led growth therefore seems to have reached its limits.

It needs a new engine of growth: in future it must rely more on

domestic demand, especially consumption. In recent years, it has been doing the opposite: consumer spending has fallen as a share of GDP, while the share of exports and investment has climbed (see chart 4). Two decades ago, consumer spending accounted for 58% of Asia's GDP. By 2007 it had fallen to 47%. Consumer spending in China is just 36% of GDP, half the American share. An analysis by CLSA, a broking firm, finds that the weight of exports in GDP now exceeds that of private consumption in six of the 11 Asian countries it tracks.



So how can Asia lift consumption? That depends on why it has been declining in the first place. The popular explanation is that it is all because frugal households have been saving a bigger slice of their income in response to uncertainty over pensions and social welfare—uncertainty that will presumably increase in a recession.

But this doesn't quite fit the facts. In many countries, notably South Korea and Taiwan, household savings have fallen relative to income in the past decade; in China they have been broadly flat. (The rise in China's savings rate comes from firms and the government, not households.)

If households are not saving more, why has consumer spending declined as a share of GDP? The answer is that wage incomes have fallen relative to GDP. In China the share of wages dropped from 53% in 1998 to 40% in 2007.

One reason for this is that job creation has slowed as governments have encouraged capital-intensive industries. Across Asia, and particularly in China, low interest rates have encouraged investment and policies such as undervalued exchange rates and subsidies have favoured manufacturing over labour-intensive services.

So if Asia is to shift the mix of growth towards consumption, the usual prescription of urging households to spend more will not be enough. A raft of government policies will have to change to lift households' share of national income. They include: reducing the bias towards capital-intensive manufacturing; speeding up financial liberalisation to lift the cost of capital; scrapping subsidies and tax breaks which favour manufacturing over services; and attacking monopolies and other barriers to services. Stronger exchange rates would also shift growth away from exports and boost households' real spending power by reducing the cost of imports in local currency terms.

In contrast, some in China are foolishly calling for a devaluation of the yuan to support the economy. This would do little to bolster exports, which have been hurt by weak external demand rather than declining competitiveness, but would hinder the necessary economic adjustment.

Even if household saving rates have been falling, they are still high, at around 20% in both China and Taiwan. This partly reflects the fact that younger populations tend to save more for retirement. An IMF study estimates that as populations age and retired workers run down their savings, this could push up consumption-to-GDP ratios in some countries by eight percentage points or more in the next decade.

Clawing it back

Policy changes can also help nudge up saving rates. In poorly developed financial systems, households find it hard to borrow and so need to save for a rainy day. Easier access to credit could reduce such saving. But the recent credit boom and bust will make governments even more cautious about financial reform.

Inadequate social-welfare nets do encourage people to save. So higher public spending on health, education and welfare support could encourage households to save less and spend more. The recent news that China plans to spend 850 billion yuan ($125 billion) over the next three years to provide basic health care for at least 90% of the population by 2011 is therefore welcome. But the details are sketchy.

After the Asian crisis, many foreigners were quick—too quick—to pronounce the regional miracle dead. Economies bounced back not just because of the appetite of American consumers, but also because Asia

still had the key ingredients of growth: rising productivity; high savings to finance investment; low import barriers to spur competition. These will help Asia remain the fastest growing region in the world. But a bigger share of those gains needs to go to workers and consumers.

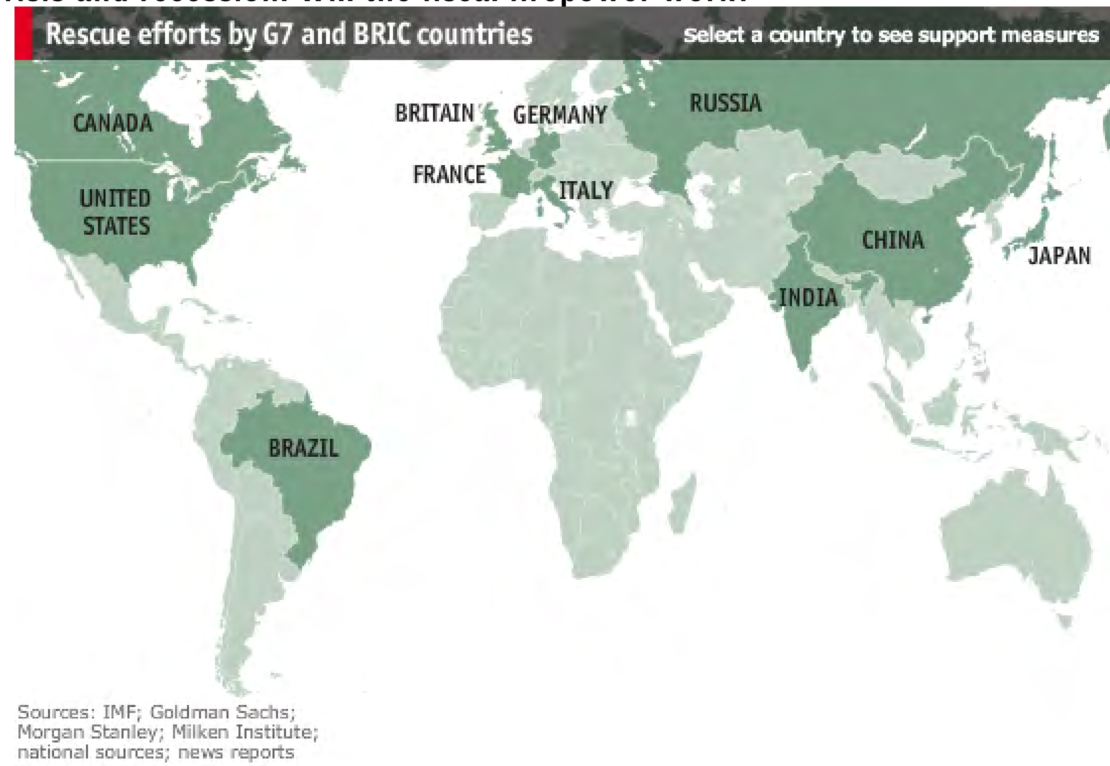
Asia's low rate of consumption and borrowing means that it has huge scope to make consumption the engine of growth over the next decade. In previous downturns, Asians were forced to take nasty medicine. Having to go out and spend would surely make a nice change.

Rescue efforts

Big government fights back

Jan 29th 2009 | WASHINGTON, DC
From The Economist print edition

Public debt is rising at its fastest pace since the second world war as governments battle financial crisis and recession. Will the fiscal firepower work?



FEW now doubt that the world economy is in its most parlous state since the 1930s. Demand is slumping across the globe as firms and consumers are battered by a pernicious, self-reinforcing bombardment of dysfunctional financial markets, falling wealth, higher unemployment and rampant fear. The IMF's latest forecasts, published on January 28th, suggest 2009 will bring the deepest global recession in the post-war era.

To stem the slump, governments are fighting back with an activism rarely seen outside wartime (see interactive graphic). In some countries, notably China, official estimates overstate the likely fiscal stimulus. But even adjusted for bureaucratic hyperbole the government response is hefty. Weighted by their economies' size, the plans of 11 big advanced and emerging economies are worth an average of 3.6% of GDP—though spread over several years. The IMF expects tax cuts and spending worth 1.5% of global GDP to kick in this year.

Illustration by S. Kambayashi



In many rich countries the stimulus has been matched—and often dwarfed—by the upfront costs of financial rescues, including the recapitalisation of banks and guarantees for troubled assets. America's Treasury has so far promised about $1 trillion (7% of GDP) for the finance industry.

Add in the tax revenues lost from slumping output and falling asset prices as well as the spending on higher unemployment benefits, and the IMF expects rich countries' combined fiscal deficit to rise to 7% of GDP in 2009, up from less than 2% in 2007. By the end of this year the developed world's gross government debt, as a share of GDP, may be 15-20 percentage points higher than it was two years ago.

Emerging economies are spilling less red ink, both because their banking industries are in less of a mess and because their stimulus plans, in general, are smaller. But they, too, will shift from a budget surplus in 2007 to a deficit of 3% of GDP. All told, public-sector debt is rising at its fastest pace since the second world war.

Most economists agree that the red ink is both unavoidable and appropriate. To prevent a steep recession becoming a depression, governments must step in to forestall financial collapse and counter the slump in private demand. Financial markets seem to agree. Yields on government bonds in most rich countries are extremely low as shell-shocked investors clamour for the safety of public debt.

Yet a few signs of skittishness are emerging. Prices of credit-default swaps on sovereign debt have risen sharply, suggesting that investors see growing risks of default. Within the rich world, risk premiums have risen dramatically for already-indebted governments such as those of Greece and Italy. Yields on America's 30-year bonds saw their biggest jump in two decades in mid-January, as investors fretted about Uncle Sam's demand for cash.

This skittishness partly reflects uncertainty about how the government debt will be financed. But the real worry is that the ultimate public price tag will be much bigger than today's figures suggest.

That seems plausible. Large as they are, the immediate costs of the financial clean-ups seem modest against the scale of the banking mess and costs of previous banking crises. So far America's government has put less than half as much public money into the financial sector, relative to the size of its economy, as Japan did in the 1990s. More will be necessary if, as is rumoured, Barack Obama's team creates a bad bank to take on troubled loans and puts more capital into banks. Goldman Sachs recently estimated that the total value of troubled American bank assets was $5.7 trillion; that makes an initial cost of several trillion dollars seem possible.

The net cost—and hence the net addition to long-term public debt—will be much smaller. On average, the IMF reckons, rich countries recover half their outlays for financial rescues. Sweden, whose banking rescue is seen as a model, recouped more than 90%. America may eventually manage something close to that, but the initial investment must be big.

Relax and spend

Unfortunately, the political cost of bailing out bankers and the huge sums involved mean that many politicians in rich countries are loth to spend heavily. History suggests that is a mistake. Failure to mend a broken financial system quickly means a longer recession; it also renders fiscal stimulus much less potent. Contrast Japan, which had numerous fiscal-stimulus packages in the 1990s, but failed to emerge from its slump until its debt problem was finally dealt with, with South Korea in 1997, which spent 13% of GDP on a large, speedy bank-rescue package.

The fiscal costs of that error can be enormous. In a recent paper Carmen Reinhart of the University of Maryland and Ken Rogoff of Harvard University estimated that the big banking crises of the post-war period, on average, raised real public debt by more than 80% of GDP. Most of that rise came not from financial rescues but from prolonged recessions and the fiscal expansions designed to combat them. Even this year, half the deterioration of the rich world’s deficits has stemmed from economic weakness.

If fiscal stimulus is no substitute for financial clean-ups, it is an important support at a time of slumping demand. But much depends on how well the plans are structured. All the big economies foresee some tax cuts, particularly for individuals. (Only a few, including Canada and Russia, plan to cut corporate taxes.) But the focus of the global fiscal boost is on spending, particularly on infrastructure.

Economic theory suggests that makes sense. When firms and consumers are gripped with uncertainty, government spending is a surer way to boost demand. Consumers and firms might save the money. The empirical evidence, however, is less than conclusive. Economists’ estimates for the “multiplier” effect of government spending and tax cuts vary widely, with equally reputable studies showing opposite results. More important, the scale of the global slump means that historical multipliers may not mean very much. That suggests a broad strategy—involving both tax cuts and spending—is prudent.

Less sensible, however, is the distribution of stimulus between countries. America’s fiscal package, at $800 billion or more, will be by far the biggest in absolute terms and one of the biggest relative to the size of its economy. Lamentably, rich creditor countries, such as Germany, are doing much less. In the emerging world China’s boldness is laudable, and fat reserve cushions have also given other emerging economies more room. But many will find their ability to borrow constrained by investors’ flight from risk—and the surge in public debt in the rich world. In its latest estimates, the Institute of International Finance, a bankers’ group, expects private-capital flows to emerging economies of only $165 billion this year, down more than 80% from 2007.

If politicians dither over bank rescues, if countries that can stimulate safely do not do enough, and if fearful investors shy away from emerging markets, the odds of a lasting recovery of the global economy seem slim. And that, in turn, will mean far bigger rises in public debt. A multi-year downturn could easily send government-debt ratios up by 30% of GDP or more.

This need not be calamitous. Governments can work off huge debt burdens without default or high inflation. During the second world war, for instance, Britain’s gross debt burden rose above 200% of GDP; America’s topped 120%. During the 1990s, fast growth and fiscal prudence allowed countries from Ireland to Canada to cut their debt levels sharply.

The difference this time is that the rich world already faces the costs of an ageing population, which promise a fiscal burden many times greater than even the darkest scenarios for the financial crisis. Right now fiscal activism is indispensable, but the consequences will be bigger and longer-lasting than many realise.

Wall Street excess

Looting stars

Jan 29th 2009 | NEW YORK
From The Economist print edition

What will it take for bankers to show a little remorse?

Reuters



They were only little bonuses

“THE road of excess leads to the palace of wisdom,” wrote William Blake. Not on Wall Street. At a time when its erstwhile titans could do with displaying contrition, signs of hubris abound. The most glaring is the sacking by Bank of America of John Thain (pictured), Merrill Lynch’s former boss, after he rushed through generous bonus payments for his investment bankers despite disastrous losses (see Buttonwood), and the revelation that he spent $1.2m refurbishing his office. Citigroup, meanwhile, has cancelled an order for a $50m executive jet, though only after flying into flak from the media and the Treasury. And, as he fights off lawsuits from angry investors, Dick Fuld, one-time leader of the now defunct Lehman Brothers, has sold his three-acre Florida estate for a princely $100—to his wife.

The recriminations over Mr Thain’s departure suggest that Wall Street’s finest were busy elsewhere when Barack Obama exhorted Americans to “set aside childish things”. While apologising for his opulent office refit, he defended the bonuses as necessary to retain talent (in this market?) and reward those unconnected to mortgage losses (whatever happened to collective responsibility?). For his part, Bank of America’s head, Ken Lewis, by now consumed with buyer’s remorse, may have known more about the handouts than he let on. His hold on his job looks fragile. Mr Thain’s role is being looked into by New York’s ever-vigilant attorney-general.

The affair could be “the last nail in the coffin” of public trust in bankers, sighs one investment-bank boss, adding that “We can now add moral bankruptcy to the financial sort.” To some, Citi’s aeroplane fiasco is equally confidence-sapping. How can a bank that owes its survival to the taxpayer think it acceptable to procure a jet that boasts “uncompromising cabin comfort” and to hold on to several others (plus a helicopter)?

The explanation may be that finance’s most recent golden age created a culture of entitlement so deep that it survives, for a while at least, even when boom turns spectacularly to bust. It is telling that fully 79% of Wall Street workers who responded to a poll by eFinancialCareers.com said they received a bonus for 2008, despite the carnage. Almost half said they were dissatisfied with the amount received.

This lack of humility could cost moneymen dear as it whips politicians and the press into an increasingly hostile alliance. The new treasury secretary, Tim Geithner, has already promised closer oversight of banks that receive public funds. Meanwhile, unearthing venality is the latest journalistic pursuit.

The loss of confidence in bankers can now be tracked. According to a financial-trust index launched this week by academics at the Kellogg School of Management and the University of Chicago, only 22% of Americans have faith in the financial system. Intriguingly, however, even fewer approve of the government’s handling of the crisis. As much as Wall Street’s erstwhile masters of the universe have helped to sully their own reputations, they remain less frowned upon than their handlers in Washington, DC.

Economist.com FINANCE & ECONOMICS

Buttonwood

The bonus racket

Jan 29th 2009
From The Economist print edition

Bank incentives are all wrong

Illustration by S. Kambayashi



"ISN'T it funny/How they never make any money/When everyone in the racket/Cleans up such a packet." That Basil Boothroyd poem was originally written about the movies, but it could just as well apply to banking.

In its last three years, Bear Stearns paid $11.3 billion in employee compensation and benefits. According to its 2007 annual report, Lehman Brothers shelled out $21.6 billion in the three years before, while Merrill Lynch paid staff over $45 billion during the three years to 2007.

And what have shareholders got from all this? Lehman's got nothing (the company went bust). Investors in Bear Stearns received around $1.4 billion of JPMorgan Chase stock, now worth just half that after the fall in the acquirer's share price. Merrill Lynch's shareholders got shares in Bank of America (BofA) which are now worth just $9.6 billion, less than a fifth of the original offer value. Meanwhile, Citigroup paid $34.4 billion to its employees in 2007 and is now valued by the stockmarket at just $18.1 billion.

All this has reinforced the idea that banking is simply a gravy train for employees. The row over the early payment of bonuses at Merrill Lynch shows yet again that insiders' interests come first (those to BofA staff, however, are likely to shrivel).

The case against banks goes something like this. Over the past 25 years, the cost of finance has been low and asset prices have generally been rising. That has encouraged banks to use more leverage in order to earn high returns on equity. The process of lending money against the security of assets, or trading assets with the banks' capital, helped to push asset prices even higher. A sizeable proportion of the profits that resulted from all this activity was then handed out to employees in the form of wages and bonuses.

But when asset prices started to fall, the whole system unravelled. Banks were forced to cut the amounts that they had borrowed, putting further downward pressure on prices. The "shadow banking system", which relied on bank finance, started to default. The result was losses that outweighed the profits built up in the good years; Merrill Lynch lost $15.3 billion in the fourth quarter of 2008 alone, compared with the $12.6 billion of post-tax profits it earned in 2005 and 2006 combined.

In effect, executives and employees were given a call option on the markets by the banking system. They took most of the profits when the market was booming and shareholders bore the bulk of the losses during the bust.

What about the efforts made to align the incentives of employees, executives and shareholders? Employees were often paid in restricted stock and thus suffered heavily when their firms collapsed; Dick Fuld, the boss of Lehman Brothers, was a prominent example. Why then were bankers not more cautious, given the risks to their own wealth?

There were two main reasons. First, their base packages (pay and cash bonuses) were sufficiently large to make them feel financially secure. That gave bankers a licence to gamble in the hope of earning the humungous payouts that would take them into the ranks of the über-wealthy. The second reason was that the bankers simply did not recognise the risks they were taking. Like most commentators (including central bankers), they thought that the economic outlook was stable and that the financial system was doing a good job of spreading risk.

Henceforth two things need to be done. The first is that the trigger for incentives (as well as the payments

themselves) need to be longer-term in nature. Bonuses could still be paid annually but based on the average performance over several years; if bankers are rewarded for increasing the size of the loan book, their pay-off should be delayed until the borrower has established a sound payment record. The effect would be to claw back profits earned by excessive risk-taking.

The second is that the banks' capital has to be properly allocated. If traders are given licence to use leverage to buy into rising asset markets, then the trading division should be charged a cost of capital high enough to reflect the risks involved.

Impossible, the banks might say: our star employees will never tolerate such restrictions. But if there is ever going to be a time to reorganise the incentive structure now must be it. A threat to quit will be pretty hollow, given the state of investment banking. And few traders will have the clout to set up their own hedge funds in today's market conditions. In any case, the greediest employees may be the ones most likely to usher in the next banking crisis. Better to wave them goodbye and wish good luck to their next employer.

Monetary policy

Trapped

Jan 29th 2009
From The Economist print edition

The ECB is not hurrying to cut interest rates—mostly for the wrong reasons

THE European Central Bank (ECB) believes it deserves a break. In a flurry of activity it took its benchmark interest rate from 4.25% in early October to 2% by mid-January. Its president, Jean-Claude Trichet, has hinted that interest rates will be kept at 2% when the bank meets on February 5th, though it may act again in March. But the euro-area economy is deep in recession and inflation is falling rapidly. Why delay?

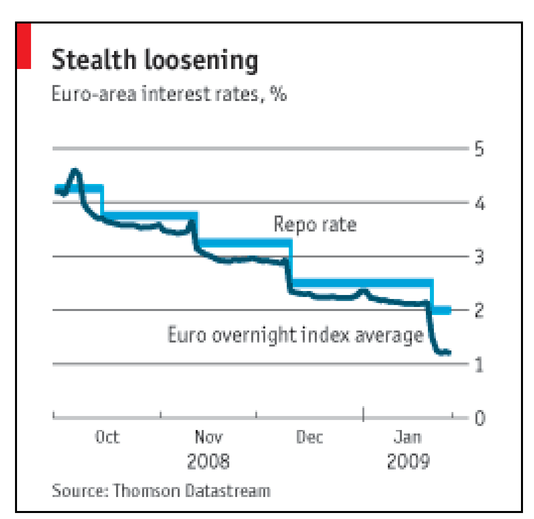
The rationale for holding off seems a bit muddled. One worry is that once interest rates fall too far, it will be hard to lift them again. Low rates make risky assets look cheap, so policymakers may hold off from raising them for too long, for fear of derailing a recovery based on rising asset values. But this is more a plea for wiser policymakers than a case against reducing rates.

Another reason for caution, voiced by Mr Trichet, is to avert a “liquidity trap”. This ambiguous bit of jargon usually refers to situations, such as when interest rates fall to zero, where orthodox monetary policy can no longer affect demand.

Some ECB rate-setters seem to suggest that a liquidity trap can be avoided simply by not reducing interest rates. Many economists fear the opposite: if policy is kept too tight and deflation takes hold it will become harder to induce spending by cutting rates. Consumers will hold back if they know that, with prices falling, their cash will buy more goods in the future. The ECB still has scope to boost demand: if it doesn’t use it, it could lose it.

Yet there may be method in the ECB’s approach. Marco Annunziata at UniCredit thinks it might be a ruse to reassure panicky markets it is in control. A hyperactive monetary policy may sometimes be harmful. John Maynard Keynes thought so: “A large increase in the quantity of money may cause so much uncertainty about the future that liquidity-preferences due to the precautionary-motive may be strengthened.” In other words, people (and banks) may cling to cash more tightly if they are spooked. This might also help explain why the bank seems happy to let market rates drift below 2% (see chart)—to talk one game while playing another.

A less worthy reason for keeping official rates on hold is that it delays the day when unorthodox policies are called for. In America the Federal Reserve hit the zero bound in December. Economists at both Goldman Sachs and Macroeconomic Advisers, a consultancy, reckon that the federal funds rate should be -6% (yes, minus six), using the “Taylor rule”, which factors in spare capacity and inflation. Unable to push the rate below zero, the Fed is prepared to use other measures, such as buying long-dated government bonds, if that helps private credit markets.



Such a policy would make the ECB uneasy. It is the world’s most independent central bank, designed to be aloof from governments, not to soil its hands by buying their debt. Finding a way to intervene in 16 sovereign-bond markets may be hard. But Thomas Mayer of Deutsche Bank suspects that is not the main barrier to unorthodox easing: “The ECB would like to remain pure. They fear that if they go down this route, they will lose their integrity.”

Hedge funds

One-and-ten

Jan 29th 2009
From The Economist print edition

Hedge fund fees are being squeezed

MIGHT two-and-twenty become one-and-ten? Since 1990 the number of hedge funds has grown by 14 times to over 7,000, but abundance has not lowered prices. Funds typically still charge clients a management fee of 2% of assets and 20% of any profits above a given hurdle. Rough calculations suggest that in the boom year of 2007, hedge funds globally received $33 billion in management fees alone—roughly equivalent to the bonus pool paid by Wall Street's securities industry.

That may now be changing. The average hedge fund lost 18% during 2008, according to Hedge Fund Research, an analysis firm. Assets fell by a quarter, reflecting both losses and client redemptions, which are expected to accelerate. To prevent fire sales, perhaps a third of funds have restricted client withdrawals. Giving clients temporary fee cuts has helped sweeten this pill.

Are permanent price cuts likely? Certainly for funds-of-funds, which act as aggregators for hedge funds and which have been tainted by their role in the Madoff scandal. One pension-scheme manager says he demanded, and quickly secured, a halving of his fee rate from a fund-of-funds. For hedge funds themselves the debacle of 2008 will mean clients start getting far tougher.

Those funds with excellent records will manage to maintain their fee rates. Big diversified managers with mediocre performance will have to cut fees to hold on to their assets. Given the "high watermarks" in place, which require that losses be recouped before performance fees can be charged, they may struggle to retain top staff, although they should at least be able to stay in business. The real threat is to smaller operators—half of all hedge funds manage less than $100m. Lower management fees may not cover their fixed costs, such as salaries, accommodation and IT. The era of hedge-fund managers being unable to pay the rent may soon be dawning.

Derivatives

Drugstore cowboys

Jan 29th 2009
From The Economist print edition

Exchanges are already muscling into the unruly over-the-counter market

THE phrase “over-the-counter” (OTC) has different meanings in medicine and finance. OTC drugs can be picked off the shelf with no prescription; OTC derivatives are traded privately between two parties rather than on an exchange. If the latter were drugs, they would probably be supplied only on prescription; they carry a big risk of unpleasant side-effects.

Compare Amaranth, which lost $6 billion trading energy futures in 2006, with Long-Term Capital Management (LTCM), which had lost $4.6 billion eight years earlier. Both were hedge funds with an aptitude for inept names (Amaranth means “undying flower”). There the similarities ended. Amaranth traded natural-gas futures on an organised exchange whereas LTCM mainly operated in OTC contracts. Amaranth’s losses barely ruffled world markets. LTCM’s caused chaos.

During the current crisis, OTC derivatives such as collateralised-debt obligations have once again created big problems. The administration of Barack Obama has them in its sights. In testimony released on January 23rd, Timothy Geithner, now America’s treasury secretary, said there needed to be more transparency and accountability. In the short term, he suggested imposing centralised clearing—something associated with exchanges—on parts of the market that can be standardised. Days earlier, the Group of Thirty, a panel of world financial experts, spoke of big shortcomings in the infrastructure supporting OTC derivatives.

Already, though, the distinction between OTC and exchange trading is blurring. As OTC volumes have slumped, efforts to make the markets more “exchange-like” have increased. Many interest-rate swaps and credit-default swaps, now traded OTC, can be standardised. Inertia and brokers’ vested interest in protecting their high-margin franchises have kept them off-exchange.

Meanwhile, the exchanges are making forays into the OTC area. In January a subsidiary of NASDAQ, an American stock exchange, launched a central clearing house for interest-rate swaps. Its London equivalent, LIFFE, has been granted regulatory approval to offer clearing of credit-default swaps, which provide insurance against default and are especially closely watched by regulators because of the surge of bad debts. Bucking a trend in the finance industry, clearing houses are still hiring staff, such as IT specialists and risk managers.

The exchanges say that by offering the flexibility of OTC markets with central clearing and automated processing, they provide the best of both worlds: customisation (within limits) coupled with reduced counterparty and operational risk. Counterparty risk is reduced since all parties work through the same clearing mechanism. That leaves less chance of gridlock when a big institution fails. Operational risks are fewer, because exchanges have been early adopters of automated processing systems, whereas OTC systems are often outdated and time-consuming. Exchanges, finally, produce a plethora of information about prices and markets, a valuable public good.

This could mark a reversal of fortune for the OTC market, where trading volumes had grown to almost $700 trillion at last count, a ninefold increase in a decade. Yet OTC products have their own blessings; they allow bankers to tailor financial products to their customers’ needs. Their relationship with exchanges need not be wholly adversarial. Financial innovations may start out in OTC markets and move to exchanges as they mature. Youth may sometimes be wild, but it should be nurtured, not suppressed.

America's mortgage agencies

Government-sponsored anxiety

Jan 29th 2009 | NEW YORK
From The Economist print edition

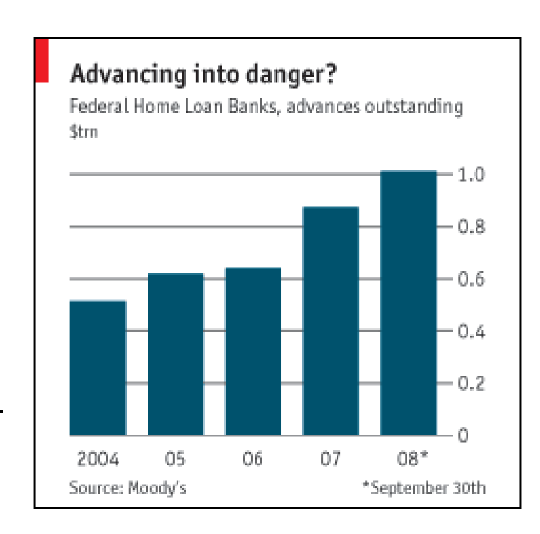
A source of support for banks when markets first crumbled is causing concern

THEY no longer hog the headlines, but America's government-sponsored mortgage agencies, Fannie Mae and Freddie Mac, continue to rack up huge losses. As they wrestle under government "conservatorship", fears are also growing over the health of their corporate cousins, the 12 Federal Home Loan Banks (FHLBs), which have so far survived the credit crunch.

Fannie and Freddie, in the red for five consecutive quarters, have said in filings that they could need $51 billion of government aid, on top of $14 billion already handed to Freddie. Freddie is in particular trouble, with negative shareholders' equity of $14 billion on September 30th.

This is worse than imagined. The duo could suck up at least $120 billion of public money this year, estimates Rajiv Setia of Barclays Capital. At this rate, they will vie with American International Group to become America's biggest money-pit.

Unlike Fannie and Freddie, the FHLBs played a subdued role in the good times. When markets dried up, however, they lent heavily. Advances to their more than 8,000 member banks rose by almost 60%, to roughly $1 trillion (see chart). The list of the biggest recipients is like a who's who of the sickly, including Citigroup, Countrywide and Washington Mutual.



This business has held up well so far. But, although no borrower has defaulted on FHLB debt, the risk of this grows as more banks fail. A more immediate worry is their $77 billion holdings of "private label" mortgage-backed securities—those not guaranteed by Fannie or Freddie. As the market value of these assets has fallen, several of them, worried that they could fall below their minimum capital requirements, have scrapped their dividends. Losses could grow as a result of "cramdowns", which allow bankruptcy judges to cut the principal owed on mortgages.

Much will depend on whether their auditors and their regulator, James Lockhart, cut them any slack. They do not have to absorb all the market losses because the securities are classed as "held to maturity". But if these impairments are deemed "other than temporary", their capital levels could be hit hard. The banks argue that they have no intention of selling the securities. But Mr Lockhart says he has been pushing for "a more rigorous process" in determining the depth of the wounds.

Mr Lockhart insists that the FHLBs are collectively solvent, and analysts agree. Their losses on mortgage securities are unlikely to exceed 10% of their combined capital of $57 billion, reckons Mr Setia, which would be painful but manageable. And if borrowers start to fail en masse, the home-loan banks will at least be first in line for repayment—a source of friction with the Federal Deposit Insurance Corporation, which supports depositors.

But any sudden requirement to crystallise paper losses could sap confidence. The FHLBs can tap public funds through a Treasury programme, but more drastic action may be required if the worst comes to the worst. Mergers among the 12 would make them bigger, but not necessarily stronger. Conservatorship is unlikely—but likelier than it was a few months ago.

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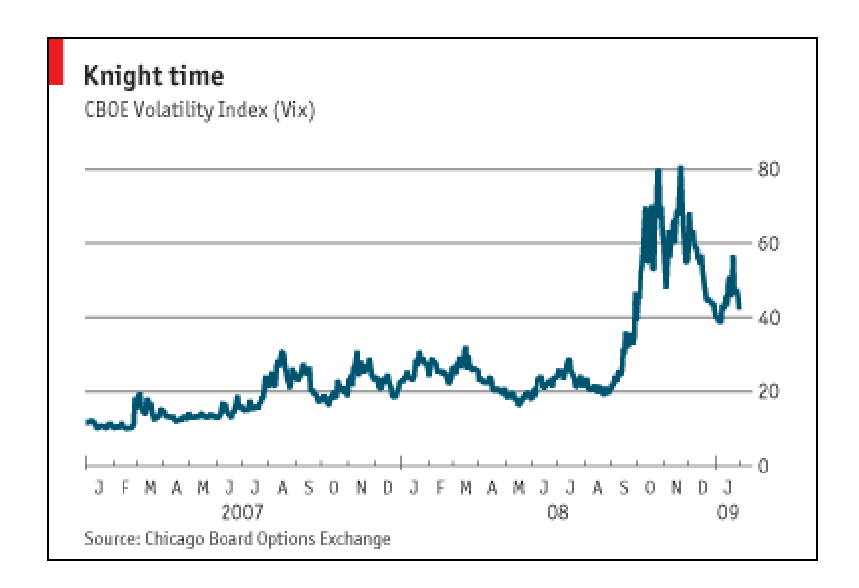
Economics focus

(Nearly) nothing to fear but fear itself

Jan 29th 2009
From The Economist print edition

In a guest article, Olivier Blanchard says that policymakers should focus on reducing uncertainty

CRISES feed uncertainty. And uncertainty affects behaviour, which feeds the crisis. Were a magic wand to remove uncertainty, the next few quarters would still be tough (some of the damage cannot be undone), but the crisis would largely go away.



From the Vix index of stockmarket volatility (see chart), to the dispersion of growth forecasts, even to the frequency of the word "uncertain" in the press, all the indicators of uncertainty are at or near all-time highs. What is at work is not only objective, but also subjective uncertainty, or what economists, following Chicago economist Frank Knight's early 20th-century work, call "Knightian uncertainty". Objective uncertainty is about what Donald Rumsfeld (in a different context) referred to as the "known unknowns". Subjective uncertainty is about the "unknown unknowns". When, as today, the unknown unknowns dominate, and the economic environment is so complex as to appear nearly incomprehensible, the result is extreme prudence, if not outright paralysis, on the part of investors, consumers and firms. And this behaviour, in turn, feeds the crisis.

It affects portfolio decisions. It has led to a dramatic shift away from risky assets to riskless assets, or at least assets perceived as riskless. It sometimes looks as if investors around the world only want to hold American Treasury bills. Why? At the start was the realisation that many of the new complex assets were in fact much riskier than they had seemed. This realisation has now morphed into a general worry about nearly all risky assets, and about the balance-sheets of the institutions that hold them. "Better safe than sorry" is the motto. Unfortunately, while the motto may make sense for individual investors, it is having catastrophic macroeconomic consequences for the world. It is triggering enormous spreads on risky assets, a credit crunch in advanced economies, and major capital outflows from emerging countries.

It affects consumption and investment decisions, and is largely behind the dramatic collapse in demand we have observed over the last three months. Sure, consumers have lost a good part of their wealth, and this is reason enough for them to retrench. But there is more at work. If you think that another Depression might be around the corner, better to be careful and save more. Better to wait and see how things turn out. Buying a new house, a new car or a new laptop can surely be delayed a few months. The same goes for firms: given the uncertainty, why build a new plant or introduce a new product now? Better to pause until the smoke clears. This is perfectly understandable behaviour on the part of consumers and firms—but behaviour which has led to a collapse of demand, a collapse of output and the deep recession we are now in.

So what are policymakers to do? First and foremost, reduce uncertainty. Do so by removing tail risks, and the perception of tail risks. On the portfolio side, establish a price, or at least a floor on the price, of the troubled assets. Ring-fence them or take them off bank balance-sheets. On the consumption side, commit to do whatever it will take to avoid a Depression, from fiscal stimulus to quantitative easing. Commit to do more in the future if necessary. Above all, adopt clear policies and act decisively. Do too much rather than too little. Delays in financial packages have cost a lot already. Further rounds of debate will stoke uncertainty and make things worse.

Second, undo the effects of uncertainty on the portfolio side, and help recycle the funds towards risky assets. The standard advice here is to return the private financial sector to health through recapitalisation. That is absolutely right, but easier said than done. And, while damage is slowly repaired, it makes sense for states to recycle part of the funds themselves. To caricature: if the world loves American Treasury bills but the funds would be more useful elsewhere, then the government should issue the bills, and use the proceeds to channel the funds where they are needed. It should buy some of the riskier assets, and return some of these funds back to emerging-market countries to offset capital outflows. This is indeed close to what America's Federal Reserve is now doing with quantitative easing at home and swap lines to foreign central banks. The only difference is that the Fed issues money rather than treasury bills in exchange for its purchases. It would make more sense for the Treasury to be involved, and to separate more clearly the role of fiscal and monetary policy, but, in the current state of play, this is a minor wrinkle. Either will do.

Retail therapy

Third, undo the effects of the wait-and-see attitudes of consumers and firms on the demand side. Get them to spend more, and have the state do some of the spending itself. Offer incentives to buy now rather than later; for example, temporary subsidies to consumers who turn in a clunker and buy a new car, a measure adopted in France. Increase spending on public infrastructure, a central component of President Barack Obama's programme. Both types of measures are indeed present in the fiscal programmes more and more countries are putting in place. If tailored and communicated well, these programmes cannot only stimulate and replace private demand, but also convince consumers and firms that they are not in for another Depression. This will ensure that they stop waiting and start spending again.

Coherent financial, fiscal and monetary measures are all needed. All three will have direct effects on demand. But, as importantly, they will help reduce uncertainty, lower risk spreads, and get consumers and firms spending again. If policymakers act decisively, private demand will recover sooner rather than later. And, within a year or less, we can be on the path to recovery.

For a discussion of this article, see www.economist.com/freeexchange

Economist.com SCIENCE & TECHNOLOGY

Embryonic stem cells

Can I serve you now?

Jan 29th 2009
From The Economist print edition

American attitudes to stem-cell therapies are changing fast

Illustration by Stephen Jeffrey



FOR the past eight years, America's government has declined to fund new research into one of the world's most promising medical technologies: the use of human embryonic stem cells to repair or replace damaged tissue in the diseased and injured. Embryonic stem cells are special for two reasons, one scientific and one ethical. The scientific reason is that they are able to turn into any of the body's myriad cell types, which is why they might be used in this way. The ethical reason is that, at the moment, harvesting them usually involves killing human embryos. The embryos in question have no future anyway (they are usually "spares" from *in vitro* fertilisation procedures). But it was this destruction of potential human life that disturbed George Bush and his supporters.

Barack Obama has promised to reverse the ban. When that happens, American academics will no longer have to watch enviously from the sidelines as their colleagues in Australia, Britain, China, the Czech Republic, Israel, Singapore and South Korea push ahead. But though the legislative wheels have yet to start turning, the mood has already shifted.

One sign of this shift came on January 23rd when the country's Food and Drug Administration (FDA) granted permission for the first clinical trial of a therapy based on human embryonic stem cells to Geron, a firm based in Menlo Park, California. Geron was able to ask for permission, and the FDA was able to grant it, because the ban does not apply to privately financed research. America, it seems, is back in the stem-cell business.

Off we go

Geron's trial is of a treatment for paralysis caused by damage to the spinal cord. Between eight and ten patients with severe spinal-cord injuries will be recruited to test this treatment for safety. At the same time both the researchers and the patients will be looking for signs of improvement in the condition. If the trial is successful, larger ones will follow.

The trick that Geron's researchers have learned is how to turn embryonic stem cells into cells called oligodendrocytes. These, in turn, generate a structure called the myelin sheath, which insulates nerves against leakage of the electrical signals that carry their messages around. Geron plans to inject its oligodendrocytes into the damaged spines of patients between one and two weeks after their injury.

Tests in rats, using human cells, have shown that oligodendrocytes injected this way can indeed help repair myelin sheaths and restore the ability of nerve cells to carry signals. The hope is that the same will happen in people. The nerve cells themselves will not be replaced, so even in principle such treatment could not help everyone with a spinal injury. Many observers do, however, see this research as a step along the road to reconnecting the brains and limbs of those with severed spinal cords, by growing new nerve cells to bridge the gap.

All new medical procedures need to be tested for safety, of course. With stem cells, the main risk is not the sort of chemical toxicity associated with a drug; rather it is of an unusual type of tumour called a teratoma. Teratomas are more or less normal bodily structures—eyes or teeth, for example—that are growing in the wrong place. They are a special risk with stem cells precisely because such cells can turn into any other sort. If the wrong genetic switch is flicked, the wrong sort of tissue results.

Another risk, though, is immune rejection. Introducing stem cells into a body is a bit like transplanting an organ: the recipient's immune system might throw a wobbly and try to destroy the intruder. Geron's patients will therefore have to spend two months taking anti-rejection drugs. Other people, though, think they may be able to get round this difficulty. The International Stem Cell Corporation (ISCo), in Oceanside, California, for one, reckons it can do so and, at the same time, deal with the ethical issue of embryo destruction.

ISCo has found a way of producing embryonic-like stem cells from unfertilised eggs. The egg is chemically stimulated to create a group of cells that form a non-viable (and unfertilised) "embryo". This, explains Kenneth Aldrich, the firm's boss, is something that could not be implanted into a woman's womb and produce a child. Nonetheless, the cells it contains have the same characteristics as stem cells.

Besides any ethical advantages this procedure may have, it could also have medical ones. Because lines of stem cells created in this way have only one parent, they are immunologically simpler than normal embryonic cells—in other words they have a smaller variety of the proteins that trigger rejection. That lack of variety, says Dr Aldrich, means it might be feasible to create a bank of stem-cell lines that could be matched to every immune type in the human population, rather as a blood bank carries blood of all the different groups (A, B, O and so on). Replacement stem cells might then be ordered off the shelf.

Nor are spinal-cord injuries the only condition lined up for treatment. Both ISCo and Advanced Cell Technology, of Los Angeles, are trying to create stem cells that could stop—and possibly reverse—a process called macular degeneration, which leads to blindness. ISCo says it hopes to start human trials later this year. Using embryonic stem cells in this way is regarded as a particularly promising route because a similar form of treatment that employs stem cells recovered from still-born children is already known to work.

Try, try, try again

The true potential of this approach is unknowable. It might yet prove too difficult to use as widely as its supporters hope. Stem-cell therapy has been suggested as a way of dealing with arthritis, angina and Parkinson's disease, as well as spinal-cord injury and blindness—a range of conditions that makes it look like a panacea. That risks disappointment and overreaction if things go wrong. But the only way to find out is to try.

Michael West, the founder of Geron and now head of BioTime, another biotechnology company, says the existing legislation has affected privately financed research as well as the public sort. Investors have been frightened off by the political debate. Once it is gone, the full brunt of America's innovative know-how, academic and private, could transform the subject, as other countries may soon find out.

Geo-engineering

Every silver lining has a cloud

Jan 29th 2009
From The Economist print edition

Plans to engineer the climate may be less effective than had been hoped

IF PEOPLE can warm the Earth, they can probably cool it too. That is the idea behind geo-engineering, which holds that besides cutting the rate at which it is turning fossil fuels into climate-changing carbon dioxide, humanity should also consider planet-wide engineering projects intended to reduce the side-effects of this combustion. All sorts of ideas have been proposed, from filling the stratosphere with reflective particles to giant space-borne parasols designed to shade the Earth from the sun. The idea of such a technological last chance, even if it sounds implausible, is a secret comfort to many of those frustrated by the lack of progress around the world in cutting emissions of greenhouse gases. Two papers published this week suggest, though, that those hopes may be misplaced.

The first, by a group of researchers from Britain's National Oceanography Centre, led by Raymond Pollard, looked at the idea of dumping iron in the oceans to promote huge blooms of phytoplankton—tiny algae that consume carbon dioxide as they grow. This approach has received a lot of interest. Though much of the carbon thus absorbed returns to the atmosphere when the plankton die, around 8-9% ends up locked away beneath the waves for decades or more. Dr Pollard's paper, which appeared in *Nature*, outlined the results of an experiment that looked at the effects of iron on the growth of phytoplankton near the Crozet Islands in the Southern Ocean.

Every year, as the days lengthen, the seas near these islands produce an enormous bloom of plankton, roughly the size of Ireland. Erosion of the islands dumps large quantities of iron in the water. The prevailing currents then carry most of this iron north, leaving the waters to the south with less. That makes the seas around the Crozet Islands an ideal natural laboratory. Dr Pollard and his colleagues found, as geo-engineers would hope, that phytoplankton blooms in the waters north of the islands were bigger and longer-lived than those to the south. More plankton means more carbon dioxide sucked from the air.

The researchers reckon that the extra iron boosted growth rates and carbon-dioxide consumption between two- and threefold. They also found the first evidence of a similar boost in the amount of carbon locked away in the deep ocean. But while the theory of iron fertilisation seems sound, the practice may be tricky: the team's results suggest that geo-engineers have overestimated the amount of carbon removed per tonne of iron by between 15 and 50 times.

AP

Similarly sobering conclusions are reached in the second paper, by Tim Lenton of the University of East Anglia and Naomi Vaughan of the Tyndall Centre for Climate Change Research, and published in *Atmospheric Chemistry and Physics Discussions*. This study attempts to rank the likely effectiveness of various geo-engineering proposals.

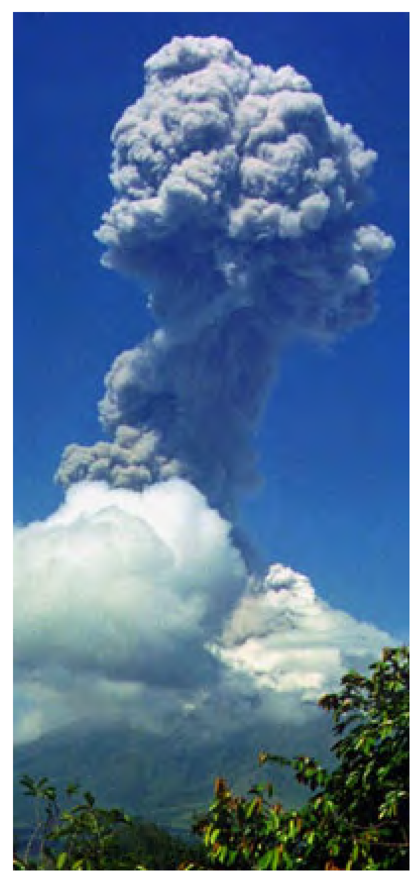
Because geo-engineering is a new field, the researchers chose to ignore trifles such as cost or practicality, and focused instead on the sheer physical limits on what can be done and how much good the different schemes would do. Top of the list is a solar shade, a gigantic umbrella in space that would shield the Earth from the sun's rays. This is both the most effective option and the most "scalable", since a hotter Earth would simply require a bigger or more opaque parasol.

The other ideas suffer from fundamental limits that stop them being scaled up indefinitely. Injecting sulphate particles into the stratosphere, for instance, would cool the Earth by reflecting more sunlight into space. (Nature has already shown that this concept can work, since volcanic eruptions that send sulphur-rich plumes into the stratosphere can temporarily alter the world's climate.) However, Dr Lenton notes that the method becomes less effective as the atmosphere becomes more saturated

with particles. At most, he reckons, the sulphate-injection approach could counteract half of the warming the world is expected to suffer over the next 100 years if carbon-dioxide emissions continue to rise unchecked.

Other options seem even less effective. Encouraging cloud formation over the oceans by spraying seawater into the air would be roughly as helpful as pumping the stratosphere full of particles. Its effects, though, would be geographically patchy. And dumping nutrients such as iron into the sea would be only one-sixth as effective as either sulphate injection or promoting the formation of clouds.

Moreover, effectiveness is only one way to rank the ideas. In theory, a solar shade could provide any amount of cooling, but the researchers estimate that it would have to have an area of 4.1m square kilometres (half the size of Brazil) to offset half the warming expected over the next century, assuming no cuts in carbon-dioxide emissions occur. A polite critic of such a plan might describe it as “ambitious”. Sulphate particles, meanwhile, survive only a few years in the atmosphere. For the sulphate-injection method to remain effective they would need to be replenished constantly for centuries—longer than the lifetime of most countries.



Sulphates to go

Then there are the side-effects. Any geo-engineering project would necessarily be enormous, and would therefore cause plenty of disruption to ecosystems. Plans to suck carbon from the air by growing trees conflict with the need to grow crops. Creating gigantic algal blooms risks using up all the oxygen in large parts of the ocean, killing anything else that lives there. These sorts of things are unlikely to go down well with environmentalists. Indeed, a group of researchers hoping to conduct more experiments on ocean fertilisation was recently ordered to stop by the German government. Ministers were worried that the experiment might have been illegal under international laws designed to protect marine wildlife, although they eventually gave the go-ahead. When it comes to the environment, there are no perfect answers.

Biomimetic materials

Does even more than a spider can

Jan 29th 2009
From The Economist print edition

How to make something useful out of spider silk

ENGINEERS who would like to exploit the accumulated evolutionary wisdom embodied in biological materials are fascinated by silk—particularly spider silk. Strands of it are stronger than steel, yet they are able to stretch by 40% of their length before they break. Silk also comes in a variety of forms; the radial strands of a web, for example, have a different composition from the circumferential ones because the stresses and strains on them are different.

The problem with the products of evolution, though, is that they are honed to do jobs for the creature they come from, not for humanity. So further engineering is needed to turn them into useful materials. And that is what David Kaplan and his colleagues at Tufts University have been trying to do.

Previous studies have identified the sequences of DNA within genes for spider-silk proteins that result in the different properties of the final products. The most important of these properties are hydrophilia (a tendency to interact with water), hydrophobia (a tendency to shun it) and the ability to link up spontaneously with other proteins and thus form larger, more complex structures.

Starting with this parts list, Dr Kaplan wondered if he could extend the range of properties of the resulting silk beyond those found in nature. He has discovered, as he describes in *Biomacromolecules*, that he can. By shuffling the order and number of the hydrophilic, hydrophobic and structure-organising sections of DNA, and then recruiting bacteria to turn the resulting artificial genes into proteins, he and his colleagues have turned out about two dozen novel forms of silk.

They also came up with the trick of getting the proteins to assemble themselves in propanol, a type of alcohol, as well as in water. The mixture of hydrophobicity and hydrophilicity in each novel protein means that the resulting materials are often different when different solvents are used, even though the underlying proteins are the same.

In particular, the researchers found that structures which would have remained thin and film-like in normal spider silk (which forms in a watery environment) thickened into tiny fibres and spheres in propanol. The spheres, they think, might be used as capsules for drugs. These could, if injected into the bloodstream, deliver a dose over a longer period than the sudden hit that comes with a traditional injection.

Some of the tougher and more water-resistant forms of silk might be employed to impregnate synthetic fibres and lightweight materials called hydrogels, in order to make them stronger and more waterproof. The more resilient materials that resulted could then be used to coat and toughen surfaces, strengthen the biologically friendly plastics employed in surgery, and create strong, lightweight components for use in aircraft, where weight is at a premium. If all goes well, then, a useful new family of polymers looks ready to be spun.

The Richard Casement internship

Jan 29th 2009
From The Economist print edition

We invite applications for the 2009 Richard Casement internship. We are looking for a would-be journalist to spend three months of the summer working on the newspaper in London, writing about science and technology. Our aim is more to discover writing talent in a science student or scientist than a scientific aptitude in a budding journalist. Applicants should write a letter introducing themselves and an original article of about 600 words that they think would be suitable for publication in the science and technology section. They should be prepared to come for an interview in London or New York, at their own expense. A small stipend will be paid to the successful candidate. Applications must reach us by February 20th. They should be sent to: casement2009@economist.com.

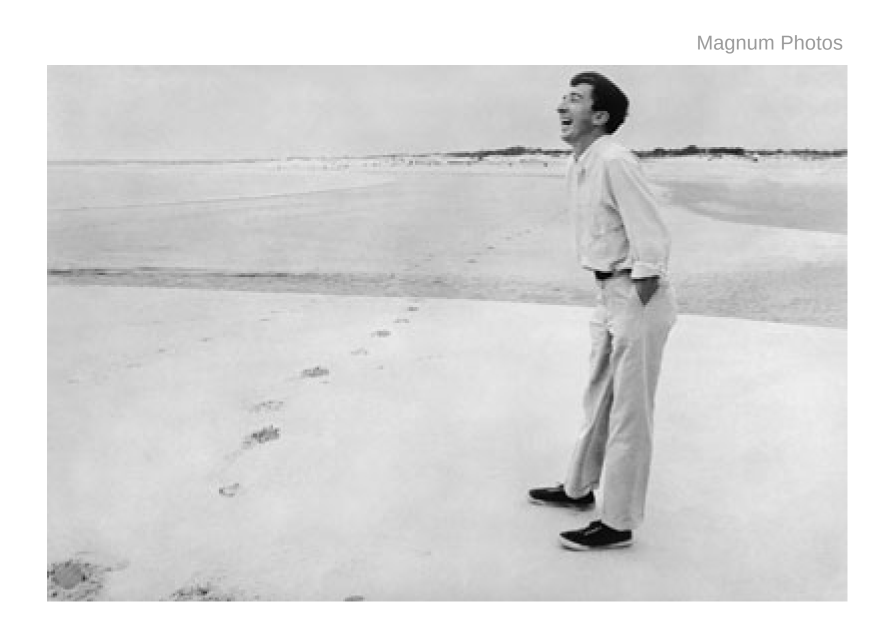
John Updike

An American subversive

Jan 29th 2009
From The Economist print edition

Three themes pervade John Updike's fiction: God, sex and America

Magnum Photos



JOHN UPDIKE, who died on January 27th at the age of 76, published 28 novels, 14 collections of short stories, nine volumes of poetry and half a century's worth of reviews on, among other things, photography, painting, golf and cartoons. With all his talent as a wordsmith, he was also a gifted cartoonist. A Protestant to his bones, Mr Updike toiled at his typewriter, writing three publishable pages a day, a book a year, working in an office each morning from 9am until lunch, convinced that everything around him, however mundane, had a deeper significance.

In this cascade of words, some work was inevitably pedestrian. But at its best, Mr Updike's writing represented the experience of his own generation of silent Americans—men, especially, who grew up in the shadow of the second world war and God-fearing austerity, only to find themselves bemused participants in the swinging sixties and the decades of consumer excess. Men liked the shiny-eyed way he wrote about sex; women, reading such lines as "She is liking it, being raped" and "As a raped woman might struggle, to intensify the deed", often judged him to be a cold-hearted exhibitionist.

It was in 1968, with his fifth novel, "Couples", that Mr Updike became suddenly famous. Sour at the decade's changing mood, his thirtysomething heroes console themselves with drink and "frugging". But it is with the four "Rabbit" books, published between 1960 and 1990, that Mr Updike will be most closely associated. His hero, Harry "Rabbit" Angstrom, is a former basketball champion turned secondhand-car dealer, a man grown bored and frustrated, his best years behind him, who is trapped in a marriage from which only extramarital sex provides any relief. To millions of readers, even to the author, Rabbit was so real that he might have been Mr Updike himself, had the hawk-nosed novelist not been saved by becoming a famous writer instead. "Rabbit was a ticket to the America all around me," he wrote in a new introduction when the tetralogy was complete. "He was *always* there for me."

Very much a Yankee, Mr Updike was the great white Protestant writer in a literary era that was dominated by Jews: Saul Bellow, Norman Mailer and Philip Roth. He liked to say that he was taught to write by Henry Green, the greatest of English Modernists, but added that this somehow implied he had "learned" writing, and "it is not a business one learns—unlearns, rather…with each day new blank paper."

Mr Updike's two main themes were God and sex. The third was America. He complained that the problem with writing about his own country was that "the slot between fantastic and drab seems too narrow", and yet Rabbit could have been born of no other earth. Mr Updike brimmed over with middle-American

prejudices. He disliked the disorder of the 1960s and 1970s, a subject brilliantly explored in “Rabbit Redux” (see review) and “Rabbit is Rich”, and he was one of the few American writers to support the Vietnam war.

Champion of the great American loser, Mr Updike used writing, not just for his readers but also for himself, to make sense of the guilt-ridden anxieties of Protestant middle America, with its residual self-righteousness mixed with the temptation represented by strip malls and motels. He disliked the New York literary scene despite writing for the *New Yorker* and Knopf, a publisher, for his whole life, and was much happier with the small-town Pennsylvania of his childhood or suburban New England. If in his private life he made fresh starts, they were always within the narrow confines of the familiar: there were two wives, (first the daughter of a Unitarian minister and then a psychologist he met socially), two major house moves (to Ipswich, Massachusetts, and then to Beverly Farms, near Boston, where he died) and three churches (the Lutheran he inherited from his parents, then Congregationalist and finally Episcopalian).

Through the ages, American literary masterpieces, such as “Moby Dick” and “The Adventures of Huckleberry Finn”, have been peopled with eccentric, rootless outsiders. Mr Updike’s lodestar was Stendhal’s definition of a novel as “a mirror that strolls along the highway”, taking in both the “blue of the skies” and “the mud puddles underfoot”. His triumph lay in taking the puritanism and practicality of the early settlers, such “enigmatic dullness”, he called it, and making it shine.

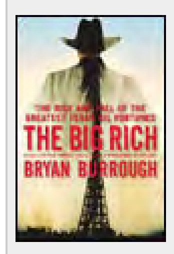
Oil in Texas

Slick and dirty

Jan 29th 2009
From The Economist print edition

WHAT'S not to enjoy about a book full of monstrous egos, unimaginable sums of money and the punishment of greed and shortsightedness by the march of events? Bryan Burrough, a former *Wall Street Journal* correspondent and one of the two writers behind the hugely successful "Barbarians at the Gate", which recounted the vast and ultimately doomed buy-out of RJR Nabisco, now offers another cautionary tale. This one is even larger in scope, and tells the story of the rise and fall of four of the giant oil families of Texas. It is a ripping, if sometimes confusing, read from start to finish. At the end of it those of less ample fortunes will feel their *Schadenfreude* richly indulged.

The Big Rich: The Rise and Fall of the Greatest Texas Oil Fortunes
By Bryan Burrough



Penguin Press; 466 pages; $29.95

"The Big Rich" charts the story of Haroldson "H.L." Hunt (and his sons, including the notorious Nelson Bunker Hunt, best known for his disastrous attempt to corner the silver market in 1979-80) and three other less well-known oil men: Sid Richardson, Clint Murchison and Roy Cullen. In their time, they were among the half-dozen richest people in America. All four were quintessential Texans: wildcatters, or independent oil producers, who lived from hand to mouth while drumming up the cash to drill for the oil that only their instincts told them lurked beneath the baked Texas soil.

Most wildcatters never found anything, or had just a lucky strike that gushed briefly before petering out. Mr Burrough's book is the story of the four who made it big. Their discoveries in the east Texas field in the miracle years of 1930-35 made the state the centre of the world's oil industry until the rise of Saudi Arabia during the second world war. At one point, Mr Burrough asserts, the United States was producing almost two-thirds of the world's black gold.

Because the book traces multiple families across the best part of a century, it is sometimes hard to follow. As well as the four who, collectively, were known for a time as "The Big Rich", there is a large cast of supporting characters. But reading it is mostly worth the effort.

The mechanics of the oil business will delight quite a few readers: there is a lot of detail about the early pseudoscience—akin really to geomancy—of working out from surface features just where pockets of oil might lie; of the dangers of drilling with cheap equipment down to depths never before attempted; and of the perilous financial and legal manoeuvring needed to snatch oil out from under the noses of the powerful oil majors. "If you're gonna owe money," reckoned Murchison, "owe more than you can pay, then the people can't afford to foreclose."

On a scale not always appreciated, the Texas oil billionaires nurtured the growth of America's radical right, financing Senator Joseph McCarthy's witch-hunt, a string of extremist newsletters (devoted to attacking such hidden dangers as the Jewish Gestapo) and even setting up an openly white-supremacist third political party, the Texas Regulars. More recently, the "Texanisation" of the Republican Party, most famously in the shape of Tom DeLay, former House majority leader, and the just-departed 43rd president, has driven the party to become more religious and outspokenly patriotic.

But it is the excesses that are most enjoyable. The 40-foot yacht deposited, by crane, in the swimming pool of one of the Big Rich by another while he was away; the jaguar smuggled into the limo of another; H.L. Hunt's spectacular polygamy, which involved him having no fewer than three families (and 14 children) dotted about the country in blissful ignorance of each other; the compulsive womanising of Murchison's son, Clint junior, who "rutted his way through an entire squad or two of Cowboy cheerleaders".

And in the end, of course, it all went bad. The last part of the book makes sobering reading. The empires

of the Big Rich, and their Neronian lifestyles, could not survive repeated collapses in the oil price. The Texas fields started to give out. The federal authorities played their part, tying up the oilmen with investigations of predatory pricing and a wiretapping scandal that almost destroyed the Hunt family. Today, the Big Rich are just humdrum rich.

Texas has fared better. No longer just an oil state, it has diversified into academia, medicine, finance and much else. And it can thank some of the oilmen—Roy Cullen in particular—for that. When the going was good, they ploughed some of their cash into the state's hospitals, universities and museums. That will stand as the Big Rich's legacy, long after the oil is gone.

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By Bryan Burrough.
Penguin Press; 466 pages; $29.95

Jaipur's Literature Festival

The power of words

Jan 29th 2009 | JAIPUR
From The Economist print edition

India's biggest book party draws thousands of visitors

CAREER diplomats and bankers rarely add glamour to arts events, but they did so at the five-day Jaipur Literature Festival in Rajasthan, India, that ended on January 25th. Two of the stars were Vikas Swarup, the diplomat-turned-author of "Q&A", a novel that became the award-winning, Oscar-nominated, British film, "Slumdog Millionaire", and Chetan Bhagat, a bank executive whose three books on life in modern India have each sold around a million copies.

Mr Swarup is India's deputy high commissioner in Pretoria and wrote "Q&A" in London in 2003. He is surprised at its success and that he is getting royalty earnings that will far exceed "many years" of his foreign ministry salary. "I just wanted to write an interesting story," he says. His second novel is a murder mystery called "Six Suspects" and the BBC has already taken an option on the film rights.

Mr Bhagat is a folk hero for India's youth and drew crowds that almost outdid those surrounding the country's leading film actor, Amitabh Bachchan, who was launching a book called "Bachchanalia" about his life in cinema. Mr Bhagat wrote two books while working for Goldman Sachs in Hong Kong—the second, "One Night @ the Call Centre", has been published in America and in Britain. Now he deals in distressed debt at Deutsche Bank in Mumbai.

Book writing is also a widespread and popular pastime among Indian diplomats. Pavan Varma, who is currently head of the foreign ministry's cultural activities and soon to be ambassador in Bhutan, is the doyen. He produced his first book, "Ghalib", about a legendary 19th-century Urdu poet, 20 years ago and has now written "over a dozen" volumes. "It's not that the foreign service necessarily gives you more time, but it does keep you [on foreign postings] out of the rat race by the sheer distance from the racing track," he says.

The four-year-old Jaipur festival, which has become India's most successful literary event, is free and open to anyone. It mixes foreign and local participation in the state rooms and grounds of Diggi Palace, a faded rambling pile built in the 1860s as a grand town house for a rural Rajasthan ruler. More than 160 writers gathered there, including many foreign visitors, among them Simon Schama, Pico Iyer, Colin Thubron and Tina Brown. The audience of several thousands—the organisers lost count at 7,000 in the middle of the five days—was mostly local. Three sessions ran continuously and concurrently, with poetry reading and concerts of sacred Muslim, Hindu and fusion music in the evenings lasting till past midnight.

Unicorns

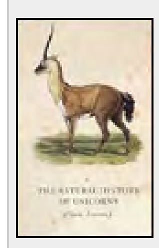
Always elsewhere

Jan 29th 2009
From The Economist print edition

TRAVELLING through Bhutan and Tibet in 1783, Captain Samuel Turner, a British army officer, took tea with the rajah of Bhutan. He described the wonders to be seen in Europe and, in return, heard of men nine feet tall and others with tails so inconveniently placed that they had to dig holes in the ground before sitting down. Most exciting of all, the rajah described a beast in his possession, a horse with a single horn in the middle of its forehead.

There are many such stories in Chris Lavers's exploration of the history and biology of the unicorn. This is a quirky, rambling book, full of lengthy detours and leisurely trips down blind alleys. Yet that is fitting. Captain Turner was neither the first traveller, nor the last, to be promised sight of a unicorn—only to discover that wherever he happened to be, it was always somewhere else. When hunting mythical beasts, it seems, the straightest path is not necessarily the quickest, and certainty increases rather than diminishes with distance and the passage of time.

The Natural History of Unicorns
By Christopher Lavers



Granta; 280 pages; £18.99. To be published in America by William Morrow in August

Buy it at
Amazon.co.uk

Some who vainly sought the unicorn made other noteworthy discoveries instead. A mention of a forest-dwelling horse known to the Mbuti pygmies of Congo, in the memoirs of Sir Henry Morton Stanley, caught the attention of Sir Henry Hamilton Johnston, a Victorian explorer and colonial administrator—and longtime dreamer of unicorns. Could Stanley's beast have a single horn in the middle of its forehead? The chance to find out came when a German showman was apprehended luring a group of Mbuti to Europe, to be displayed at the 1900 Paris Exhibition. Johnston travelled to Congo with the repatriation party, and was rewarded by the discovery of a new creature, the okapi. Sadly, the females have no horns and the males two, but the discovery did make headlines around the world.

Illustration by Daniel Pudles



Mr Lavers describes the unicorn's many relatives, both fabulous and mundane. The narwhal has a single horn (actually a giant protruding tooth) and if unicorns existed in the sea, went the argument in medieval times, surely they also existed on land. A variety of shy, fleet, bi-horned mammals appear uni-horned in profile and from a distance—the Tibetan chiru, the Arabian oryx—and the legend of the unicorn gained strength from the use of the horns of certain animals to detect, or counteract, poisons, a function so valuable that horns were sold singly. More distant on the family tree was the legendary roc, a vast, elephant-eating bird, which shared some pseudo-palaeontology with mythical horned beasts. To some, the arched snout and horns of skeletal Ice Age woolly rhinoceroses suggested not a vast land mammal, but the beak and claws of a giant bird.

Baron Cuvier, a 19th-century zoologist, thought the unicorn not only mythical, but impossible, for its single central horn would have to grow out of a suture in the skull. But he was mistaken about that: horns grow from buds in the flesh, not from the bone. In 1933 a biologist at the University of Maine removed those buds from their normal position on a day-old Ayrshire bull's forehead and replaced them, one on top of the other, in its centre. Thus was made a real live unicorn to join the many other varieties: the biblical one, small and meek; the heraldic one, noble; and the New Age one, airbrushed, gleaming white and crystal-festooned.

The Natural History of Unicorns.
By Christopher Lavers.
Granta; 280 pages; £18.99. To be published in America by William Morrow in August

New fiction

Simon Mawer's dream palace

Jan 29th 2009
From The Economist print edition

The Glass Room
By Simon Mawer



Little, Brown; 405 pages; £16.99

Buy it at
Amazon.com
Amazon.co.uk

THE notion of a house, or more specifically a room, as the principal character in a novel is an odd one. But this is the case in Simon Mawer's eighth work of fiction, "The Glass Room", which is inspired by the Tugendhat Villa in Brno and spans 60 years of Czechoslovakia's turbulent history.

In 1929, newlyweds Viktor and Liesel Landauer employ Rainer von Abt to design them a house that becomes a masterpiece of modernist architecture. The centrepiece is the glass room; an open space filled with light that reflects their dream of living in "a state in which being Czech or German or Jew would not matter". Yet, as a result of Viktor's Jewish heritage, in 1939 the Landauers are forced to flee the country in the face of a Nazi invasion.

The family moves first to Switzerland, then slowly across Europe towards Bilbao, before sailing to America. Meanwhile, the house changes occupiers as fast as the country changes names. The glass room becomes a scientific centre for racial studies where a Nazi scientist, Werner Stahl, attempts to discover "the systematic measurement of what defines human and subhuman". The space then provides a refuge from bombing raids, is liberated by the arrival of the Soviet army and, during the communist era, acts as a rehabilitation unit for children with polio. Each new occupant is affected by the glass room's quiet power; as lives are shattered around it, it remains a place of dreams. With the fall of communism the house becomes a museum, where the ghosts from its past can finally be reunited.

Mr Mawer likes to write about ideas, which makes him unusual among British novelists. "The Glass Room" is a carefully constructed book, beautifully written. If there is a flaw, it is a lack of contact with the characters—the only figure portrayed with feeling is the flippant and omnisexual Hana Hanakova, who becomes the real survivor of the story. However, this narrative distance emphasises the fact that to the glass room, indifferent and ageless, people pass through "like summer mayflies with their gossamer wings and delicate tails and ephemeral lives". The novel succeeds as a reminder of the transient nature of human existence.

The Glass Room.
By Simon Mawer.
Little, Brown; 405 pages; £16.99

The YSL / Pierre Bergé sale

Scattered to the winds

Jan 29th 2009 | PARIS
From The Economist print edition

The auction of a great French collection is likely to make art-market history

BEHIND an unassuming courtyard door off the rue de Babylone on the *rive gauche* in Paris, an art-and-design collection like no other awaits dispersal. Yves Saint Laurent, a French fashion designer who died last June at the age of 71, and Pierre Bergé, his business and personal partner, assembled the collection together over 50 years. On February 23rd, in an auction that will last three days, Christie's will start bringing down the hammer on 733 objects. This is likely to be the biggest single-owner sale in auction history and, potentially, a coup for the Paris art market, which recently suffered the humiliation of being overtaken, in auction turnover, by Hong Kong (New York and London still rank first and second).

Saint Laurent's grand salon lies at the end of an oval lacquered hallway. A glance to one side of the long rectangular room takes in a large cubist Picasso, a delicate painting of a countess by Jean Auguste Dominique Ingres, an iconic mechanical nude by Fernand Léger, an odd portrait of two children by Théodore Géricault and a rare wooden primitivist sculpture by Constantin Brancusi that was once in Léger's own collection. In the mirror behind the Brancusi are reflected three more Léger paintings and a splendid Giorgio de Chirico of a man with a tailor's dummy (pictured below). The combined low estimate for these nine pieces is €73m ($94.8m).

These works hang above a covetable array of furniture by designers from the Art Deco period (Gustave Miklos, Pierre Legrain, Eileen Gray and Jean Dunand), as well as small 17th-century statues of muscular Greek gods and rampant animals and other *objets d'art*. Almost every piece boasts a stellar cast of previous owners. The only unsightly thing in the room is Moujik IV, Saint Laurent's pet bulldog, who greets visitors with an indolent sniff.

From the grand salon, the visitor passes through the music room, lined with mirrors by Claude and François-Xavier Lalanne that Saint Laurent and Mr Bergé commissioned in 1974, then down the stairs past both an Egyptian sarcophagus flanked by early 16th-century depictions of John the Baptist and a room of curiosities, including cameos, chalices, crosses and Medusa heads. Then comes Saint Laurent's personal library—a light, airy room containing, among other things, three magnificent Mondrian canvases dating from 1918, 1920 and 1922. The overall effect is one of glamour, intelligence and luxury, just as one might expect from the team that invented serious fashion. Saint Laurent regularly evoked high art in his work, most overtly with his Mondrian dress of 1965, and he was the first fashion designer to enjoy his own retrospective at the Metropolitan Museum of Art.

The collection is so renowned, and the works combine so well, that it is not surprising that Abu Dhabi tried to pre-empt the auction by buying it all. Mr Bergé acknowledges that a dealer approached him on behalf of a Middle Eastern buyer, but is unwilling to elaborate. Mr Bergé, however, is set on dismantling the collection for emotional as well as financial reasons. The auction is a spectacular homage and final goodbye to an intimate collaboration.

Christies

Additionally, Mr Bergé may not want it to overshadow the collection of 5,000 *haute couture* outfits and 15,000 accessories, sketches and related objects whose preservation and promotion are the raison d'être of the Pierre Bergé-Yves Saint Laurent Foundation. In fact, half of the auction proceeds will go the foundation (the other half will go to Mr Bergé, and to a variety of charity projects including scientific research into AIDS).

Almost as intriguing as the pieces themselves are the machinations involved in bringing them to market. Many dealers assumed that the collection would be consigned to Sotheby's, which sold the contents of Mr Bergé's Pierre Hotel apartment in New York in 2004. Moreover, Mr Bergé is not enamoured of François Pinault, the owner of Christie's, who also happens to own the Gucci Group, which bought the YSL brand in 1999

and assigned Tom Ford as creative director—an unhappy experience for Saint Laurent.


A couturier's dream

Mr Bergé is a pragmatist, however. He became frustrated, he says, with the "discussions from ocean to ocean" between Paris and Sotheby's New York headquarters. Meanwhile, he began quiet talks with Christie's French vice-president, François de Ricqlès, in October 2007. Mr de Ricqlès prevailed and nine months later Mr Bergé signed a slim six-page contract with Christie's that contained neither valuations nor a list of works, but, crucially, included a substantial cash advance.

Now Christie's is preparing for *la grande vente*, which will consist of three evening-sales and two day-sales presided over by eight auctioneers. Prominent art historians, such as Yve-Alain Bois from Princeton University, have written essays for the glossy five-volume catalogue, which retails for €200. Highlights from the collection were exhibited in November in New York; others will be displayed in London until February 4th, then Brussels in mid-February, before reaching the Grand Palais itself. There, the exhibition will be open to the public from 9am to midnight over the weekend before the sale. The Grand Palais activities alone will cost Christie's more than €1m.

Beauty and the buyers

The scale and ambition of the auction hark back to a rosier art market. Although Christie's has offered Mr Bergé no guarantees and the sale estimates are considered reasonable (a few have even been revised downwards since the autumn) the sheer volume of work on offer is a lot for the market to digest.

None of that seems to worry Mr Bergé. "Maybe I'm presumptuous, but the majority of the lots are so beautiful and so important that I don't think the crisis exists really for that," he says. "Even if the sale is not as successful as it might have been two years ago, it will bring in money enough for its objectives." Christie's is expecting at least 100 *gros acheteurs*, and it is confident that bidders will be unable to resist the combination of quality and fame. "What is more secure today than a timeless masterpiece with an illustrious provenance?" asks Mr de Ricqlès. "We are cautious, but we expect some world-record prices."



OPINION

Correction: Gérard Prunier

Jan 29th 2009
From The Economist print edition

In our recent review of two books about the war in central Africa, ("Bloody history, unhappy future", January 24th), we should have mentioned that Gérard Prunier's work, "Africa's World War: Congo, the Rwandan Genocide, and the Making of Continental Catastrophe", is published in Britain by C. Hurst under the title, "From Genocide to Continental War: The 'Congolese' Conflict and the Crisis of Contemporary Africa"; £30.

John Mortimer

Jan 29th 2009
From The Economist print edition

Sir John Mortimer, barrister and freedom-fighter, died on January 16th, aged 85

Getty Images



EVERY true-born Englishman knows that the law is an ass. Rules are better honoured in the breach than the observance. Judges are best represented in a chorus line at the D'Oyly Carte. The English constitution is a vague formulation in someone's head, and that foundation of English liberties, Magna Carta, is best known for banning eel-traps in the Thames. The firm clip of the law is for the other fellow. Behind the furled umbrellas and decorum, Englishmen are anarchists. Or, as John Mortimer liked to think of them, votaries of "my darling" Prince Kropotkin.

Mr Mortimer's great service to his country was to sum up in one person both the weight of the law and a sharp, rollicking scepticism of it. He was an eminent lawyer, entering chambers in 1948 and becoming, in time, a Queen's Counsel and a master of the bar. Few excelled him in cross-examination (the art of which, he liked to say, was "not to examine crossly"). Yet the law was only his day job, giving him the money and the material to write novels. At the bar he dressed scruffily, lest anyone take him for a conventional lawyer. He made fun of the "old sweethearts" on the bench, who would pass a death sentence and then go out for buttered muffins. And as for the law itself, "the great stone column of authority which has been dragged by an adulterous, careless, negligent and half-criminal humanity down the ages",

> [it] is a subject which, I may say, never interested me greatly. People in trouble, yes. Bloodstains and handwriting, certainly…Winning over a jury, fascinating. But law! The only honourable way to pass a law exam is to make a few notes on the cuff and take a quick shufti at them during the occasional visit to the bog.

Those words were not exactly his, but those of Horace Rumpole (seen above right, played by Leo McKern), whose adventures at the criminal bar Mr Mortimer tirelessly depicted in books and TV plays from 1975 onwards. He denied that Rumpole was entirely himself. There was much of his barrister-father in him, especially in his habit of quoting poetry to ward off unwelcome conversation, as well as borrowings from colourful colleagues. Rumpole was a cheroots-and-cheap-claret man ("Pommeroy's claret keeps me astonishingly regular"), where Mr Mortimer favoured cigars and, at the dawn of the writing day, champagne. He often lost his cases, where Mr Mortimer was notably successful. Home for Rumpole was a mansion flat off Gloucester Road, where he lived in a state of miserable, snappish fidelity to Hilda, "She Who Must be Obeyed". Mr Mortimer graced the well-heeled, pretty Chilterns near Henley-on-Thames, where children, stepchildren, a love-child, two wives called Penelope and the "Mortimer-

ettes", a claque of intelligent, charmed women, paid court to him and he to them.

A golden thread

Where Rumpole and Mr Mortimer fused together was in their sense of how lawyers should behave. Both were freedom-fighters. They refused to prosecute: their role was to defend the individual against the weight and follies of the law. Rumpole, grubbing round the Old Bailey cells with their "perpetual smell of cooking", refused to let his clients plead guilty while the smallest doubt remained. He liked to quote Lord Sankey's words on the presumption of innocence, the "single golden thread" that ran through English law.

Mr Mortimer, also tracing that thread, took on the most celebrated free-speech cases of the 1970s, and won them all. Largely thanks to him, the lord chamberlain's censoring hand was lifted from the theatre. Thanks to him, Englishmen could read "Lady Chatterley's Lover" and "Inside Linda Lovelace", could see Rupert Bear with an erection in *Oz* magazine, and could endure a Roman soldier's tryst with the body of Jesus in *Gay News*. Mr Mortimer hated pornography. But "Liberty is allowing people to do things you disapprove of."

He took that conviction into politics, too. It led him to support foxhunting and to resume smoking in old age, just to defy the ban. He played the devil's advocate on behalf of freedom everywhere, from the Oxford Union to the dinner table. Bishops were a favourite target, rapiered for the "absurdity" of life and the worse absurdity of heaven, which had to resemble "the lounge of a Trusthouse Forte hotel". People, he thought, should be regularly shocked. Offence "makes society move".

All this, he admitted, came close to anarchism. Yet at its base was something different. He took up the law, which made all else possible, out of obedience to his father. Clifford Mortimer was blinded when John was 13, yet continued his law practice and his life as though nothing had happened. For his son—as he explained in his play, "A Voyage Round My Father", in 1971—a career at the bar was an extension of all the other duties he assumed for his demanding, unseeing parent, from tying up the dahlias and trapping earwigs to handing him his boiled egg, or his coat.

> He walked with his hand on my arm. A small hand, with loose brown skin. From time to time, I had an urge to pull away from him, to run into the trees and hide…But then his hand would tighten on my sleeve…He was very persistent…

The freedom-fighter defied most laws but not this one, family love.

Overview

Jan 29th 2009
From The Economist print edition

The **Federal Reserve** maintained its target for overnight interest rates at 0-0.25% on January 28th. The Fed said it was prepared to buy long-dated government bonds if necessary, but did not commit itself to doing so.

The index of **American** consumer confidence published by the Conference Board, a research firm, edged down in January to 37.7, a new low for the series, which dates back to 1967. House prices fell by 18.2% in the year to November, according to the S&P/Case-Shiller index of house prices in 20 big cities. Low prices offered by distressed sellers are tempting more buyers. Sales of existing homes jumped by 6.5% in December, according to the National Association of Realtors.

Britain's GDP fell by 1.5% in the fourth quarter, according to a preliminary estimate. It was 1.8% lower than a year earlier.

Confidence among businessmen in **Germany** is low but stable, according to Ifo, a research institute in Munich. Its business-sentiment index edged up from 82.7 to 83.0 in January. The gauge of **Italian** business confidence by ISAE, a Rome research group, fell to its lowest level since at least 1991.

Consumer prices in **Australia** fell by 0.3% in the three months to December, the biggest quarterly decline since 1997. The drop took the annual inflation rate down to 3.7%, from 5% in the third quarter.

Israel's central bank announced that it was cutting its benchmark interest rate by 0.75 percentage points, to 1%.

Output, prices and jobs

Jan 29th 2009
From The Economist print edition

Output, prices and jobs

% change on year ago

	Gross domestic product				Industrial production	Consumer prices			Unemployment
	latest	qtr*	2008†	2009†	latest	latest	year ago	2008†	rate‡, %
United States	+0.7 Q3	-0.5	+0.9	-1.2	-7.8 Dec	+0.1 Dec	+4.1	+3.7	7.2 Dec
Japan	-0.5 Q3	-1.8	nil	-1.4	-16.6 Nov	+1.0 Nov	+0.6	+1.5	3.9 Nov
China	+6.8 Q4	na	+9.1	+6.0	+5.7 Dec	+1.2 Dec	+6.5	+5.9	9.0 2008
Britain	-1.8 Q4	-5.9	+0.6	-1.7	-6.9 Nov	+3.1 Dec§	+2.1	+3.5	6.1 Nov††
Canada	+0.5 Q3	+1.3	+0.4	nil	-3.4 Oct	+1.2 Dec	+2.4	+2.2	6.6 Dec
Euro area	+0.6 Q3	-0.7	+0.7	-1.4	-7.7 Nov	+1.6 Dec	+3.1	+3.2	7.8 Nov
Austria	+1.5 Q3	+0.6	+1.6	-1.3	+0.7 Nov	+1.3 Dec	+3.6	+3.0	3.8 Nov
Belgium	+1.3 Q3	+0.4	+1.3	-0.7	-5.3 Oct	+2.6 Dec	+3.1	+4.4	10.8 Dec‡‡
France	+0.5 Q3	+0.5	+0.7	-1.0	-9.0 Nov	+1.0 Dec	+2.6	+3.0	7.9 Nov
Germany	+0.8 Q3	-2.1	+1.0	-1.4	-6.3 Nov	+0.9 Jan	+2.8	+2.6	7.8 Jan
Greece	+3.1 Q3	+2.0	+2.6	+1.4	-5.9 Nov	+2.0 Dec	+3.9	+4.0	7.4 Oct
Italy	-0.9 Q3	-2.1	-0.5	-1.2	-9.7 Dec	+2.2 Dec	+2.6	+3.4	6.7 Q3
Netherlands	+1.8 Q3	+0.1	+1.6	-0.6	-6.2 Nov	+1.9 Dec	+1.9	+2.3	3.9 Dec††
Spain	+0.9 Q3	-0.9	+1.0	-1.3	-17.2 Nov	+1.4 Dec	+4.2	+4.3	13.4 Nov
Czech Republic	+4.2 Q3	+3.8	+4.2	+0.8	-17.4 Nov	+3.6 Dec	+5.4	+6.5	6.0 Dec
Denmark	-1.2 Q3	-1.9	-0.4	-1.2	-6.8 Nov	+2.4 Dec	+2.3	+3.4	2.1 Dec
Hungary	+0.8 Q3	-0.3	+0.8	-3.0	-12.0 Nov	+3.5 Dec	+7.4	+6.2	7.8 Nov††
Norway	+0.6 Q3	-2.8	+1.8	-0.2	+0.1 Nov	+2.1 Dec	+2.8	+3.8	2.9 Nov***
Poland	+4.8 Q3	na	+5.1	+2.9	-4.4 Dec	+3.3 Dec	+4.0	+4.3	9.5 Dec‡‡
Russia	+6.2 Q3	na	+6.0	+1.0	-10.8 Dec	+13.3 Dec	+11.9	+14.1	7.7 Dec‡‡
Sweden	nil Q3	-0.4	+0.6	-0.6	-11.9 Nov	+0.9 Dec	+3.5	+3.4	6.4 Dec‡‡
Switzerland	+1.7 Q3	+0.1	+1.6	-0.6	+0.7 Q3	+0.7 Dec	+2.0	+2.4	2.8 Dec
Turkey	+0.5 Q3	na	+2.3	+0.4	-13.9 Nov	+10.1 Dec	+8.4	+10.5	10.3 Q3‡‡
Australia	+1.9 Q3	+0.3	+2.0	+0.8	+3.8 Q3	+3.7 Q4	+3.0	+4.4	4.5 Dec
Hong Kong	+1.7 Q3	-2.0	+3.0	-3.0	-6.7 Q3	+2.1 Dec	+3.8	+4.2	4.1 Dec††
India	+7.6 Q3	na	+5.6	+5.2	+2.4 Nov	+10.4 Nov	+5.5	+8.1	6.8 2008
Indonesia	+6.1 Q3	na	+6.1	+3.5	+1.9 Nov	+11.1 Dec	+4.9	+10.4	8.4 Aug
Malaysia	+4.7 Q3	na	+5.6	+3.2	-7.7 Nov	+4.4 Dec	+2.4	+5.7	3.1 Q3
Pakistan	+5.8 2008**	na	+6.0	+1.4	-2.2 Oct	+23.3 Dec	+8.8	+20.8	5.6 2007
Singapore	-3.7 Q4	-16.9	+1.9	-2.9	-13.5 Dec	+4.3 Dec	+4.4	+6.6	2.2 Q3
South Korea	-3.4 Q4	-20.8	+4.1	-2.8	-14.1 Nov	+4.1 Dec	+3.6	+4.9	3.3 Dec
Taiwan	-1.0 Q3	na	+2.3	-2.9	-32.3 Dec	+1.2 Dec	+3.3	+3.8	5.0 Dec
Thailand	+4.0 Q3	+2.3	+3.4	-1.0	-6.6 Nov	+0.4 Dec	+3.2	+5.5	1.1 Sep
Argentina	+6.2 Q3	+5.4	+5.5	-1.8	-7.2 Nov	+7.2 Dec	+8.5	+8.6	7.8 Q3‡‡
Brazil	+6.8 Q3	+7.4	+5.3	+2.4	-6.2 Nov	+5.9 Dec	+4.5	+5.8	6.8 Dec‡‡
Chile	+4.8 Q3	-0.2	+3.5	+1.0	-5.7 Nov	+7.1 Dec	+7.8	+8.7	7.5 Nov††‡‡
Colombia	+3.1 Q3	+2.9	+3.2	+2.0	-13.3 Nov	+7.7 Dec	+5.7	+7.1	10.8 Nov‡‡
Mexico	+1.6 Q3	+2.6	+1.8	-1.4	-5.4 Nov	+6.5 Dec	+3.8	+5.1	4.3 Dec‡‡
Venezuela	+4.6 Q3	na	+4.2	-3.0	+2.7 Sep	+30.9 Dec	+22.4	+30.5	7.2 Q3‡‡
Egypt	+5.9 Q3	na	+7.2	+5.1	+7.3 Q3	+18.3 Dec	+6.9	+18.4	8.6 Q3‡‡
Israel	+5.1 Q3	+2.3	+4.1	+0.9	+1.8 Oct	+3.8 Dec	+3.4	+4.5	5.9 Q3
Saudi Arabia	+3.5 2007	na	+6.0	+3.0	na	+9.5 Nov	+4.8	+9.4	na
South Africa	+2.9 Q3	+0.2	+3.5	+2.5	-4.4 Nov	+9.5 Dec	+9.0	+11.4	23.2 Sep‡‡
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*									
Estonia	-3.5 Q3	na	-2.3	-3.3	-17.7 Nov	+7.0 Dec	+9.6	+10.4	8.3 Nov
Finland	+1.3 Q3	+0.4	+1.6	-1.3	-10.1 Nov	+3.5 Dec	+2.6	+4.1	6.6 Dec
Iceland	-0.8 Q3	-5.5	-0.5	-9.7	+0.4 2007	+18.6 Jan	+5.8	+13.8	4.8 Dec‡‡
Ireland	+0.1 Q3	+4.7	-2.9	-4.0	+2.8 Nov	+1.1 Dec	+4.7	+4.2	8.3 Dec
Latvia	-4.6 Q3	na	-1.8	-8.0	-13.9 Nov	+10.5 Dec	+14.1	+15.4	9.0 Nov
Lithuania	-1.5 Q4	-9.3	+4.4	+1.6	na	+8.5 Dec	+8.1	+11.2	5.7 Dec‡‡
Luxembourg	-0.3 Q3	-5.5	+2.5	+1.5	-9.8 Oct	+1.1 Dec	+3.4	+3.6	4.7 Nov‡‡
New Zealand	-1.4 Q3	-2.7	-0.9	-1.9	-0.5 Q3	+3.4 Q4	+3.2	+4.3	4.2 Q3
Peru	+5.1 Nov	na	+9.1	+5.5	+5.1 Nov	+6.7 Dec	+3.9	+5.8	7.9 Nov‡‡
Philippines	+4.5 Q4	+4.1	+4.3	+1.4	+2.2 Oct	+8.0 Dec	+3.9	+9.6	6.8 Q4‡‡
Portugal	+0.6 Q3	-0.5	+0.4	-0.8	-6.2 Nov	+0.8 Dec	+2.7	+2.6	7.7 Q3‡‡
Slovakia	+7.0 Q3	na	+6.8	+2.0	-7.1 Nov	+4.4 Dec	+3.4	+4.6	8.4 Dec‡‡
Slovenia	+3.8 Q3	na	+4.2	+1.4	-12.0 Nov	+2.1 Dec	+5.6	+5.7	6.7 Nov‡‡

*% change on previous quarter, annual rate. †*The Economist* poll or Economist Intelligence Unit estimate/forecast. ‡National definitions.- §RPI inflation rate 0.9% in Dec. **Year ending June. ††Latest three months. ‡‡Not seasonally adjusted. ***Centred 3-month average

Sources: National statistics offices and central banks; Thomson Datastream; Reuters; Centre for Monitoring Indian Economy; OECD; ECB

The Economist commodity-price index

Jan 29th 2009
From The Economist print edition

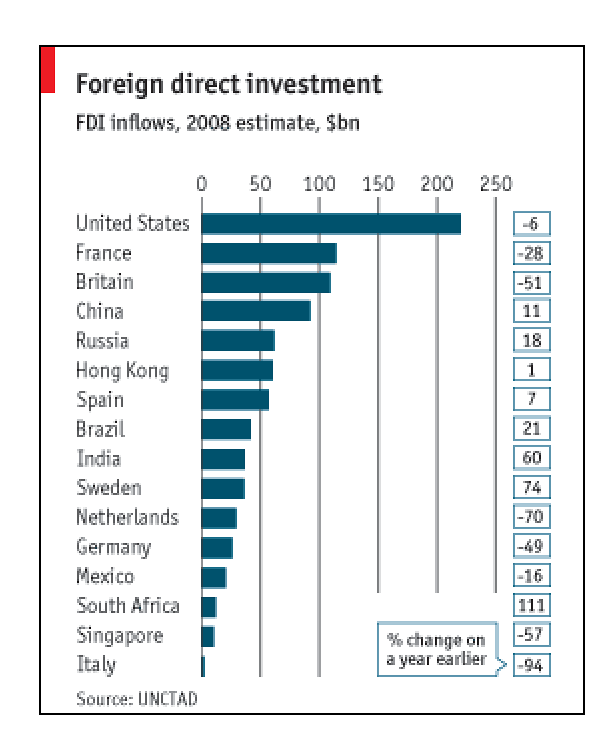
The Economist commodity-price index
2000=100

	Jan 20th	Jan 27th*	% change on one month	% change on one year
Dollar index				
All items	158.8	160.9	+3.4	-28.8
Food	187.7	190.9	+2.6	-15.9
Industrials				
All	121.4	122.2	+5.1	-45.7
Nfa†	114.0	116.4	+3.1	-35.8
Metals	125.4	125.3	+6.2	-49.6
Sterling index				
All items	172.4	172.2	+5.3	-1.5
Euro index				
All items	113.7	113.0	+11.1	-21.0
Gold				
$ per oz	862.10	900.05	+3.3	+0.8
West Texas Intermediate				
$ per barrel	38.53	42.05	+7.3	-53.1

*Provisional †Non-food agriculturals.

Foreign direct investment

Jan 29th 2009
From The Economist print edition



Foreign direct investment (FDI)—the purchase of factories, offices and other assets by foreign companies—shrank by more than a fifth last year, according to new estimates from UNCTAD. The factors that led firms to cut back capital spending at home, such as scarce credit, weak profits and uncertainty about demand, also hurt cross-border investment. The worst-hit countries were rich ones, particularly in Europe. FDI into Britain and Germany was around a half of its 2007 level. In Italy it fell by 94%. Flows into the United States, the biggest recipient of FDI, held up rather better. Big emerging markets, such as Brazil, China, India and Russia, saw FDI increase last year but may be in for a rocky 2009.



Trade, exchange rates, budget balances and interest rates

Jan 29th 2009
From The Economist print edition

Trade, exchange rates, budget balances and interest rates

	Trade balance* latest 12 months, $bn	Current-account balance		Currency units, per $		Budget balance % of GDP 2008†	Interest rates, %	
		latest 12 months, $bn	% of GDP 2008†	Jan 28th	year ago		3-month latest	10-year gov't bonds, latest
United States	-833.1 Nov	-697.9 Q3	-4.5	-	-	-3.2	0.27	2.65
Japan	+47.3 Nov	+167.1 Nov	+3.8	89.7	107	-3.2	0.61	1.26
China	+295.1 Dec	+371.8 2007	+10.2	6.84	7.19	-0.1	1.38	2.93
Britain	-178.6 Nov	-45.6 Q3	-2.4	0.70	0.50	-5.3	2.13	3.85
Canada	+47.3 Nov	+19.2 Q3	+1.0	1.21	1.00	0.3	0.85	3.23
Euro area	-52.0 Nov	-88.9 Nov	-0.3	0.76	0.68	-1.6	2.12	3.23
Austria	-0.6 Oct	+16.8 Q3	+2.8	0.76	0.68	-1.0	2.12	4.10
Belgium	+7.9 Sep	-8.2 Sep	+0.1	0.76	0.68	-0.6	2.14	4.28
France	-83.3 Nov	-58.7 Nov	-1.8	0.76	0.68	-3.0	2.12	3.72
Germany	+267.2 Nov	+244.3 Nov	+6.6	0.76	0.68	0.3	2.12	3.23
Greece	-68.5 Oct	-52.6 Nov	-10.3	0.76	0.68	-3.2	2.12	5.87
Italy	-18.7 Nov	-72.2 Oct	-2.9	0.76	0.68	-2.8	2.12	4.57
Netherlands	+55.4 Nov	+67.6 Q3	+6.7	0.76	0.68	1.0	2.12	3.94
Spain	-149.5 Oct	-164.1 Oct	-9.8	0.76	0.68	-3.3	2.12	4.34
Czech Republic	+4.8 Nov	-6.6 Nov	-2.7	20.8	17.6	-1.9	2.74	4.31
Denmark	+6.2 Nov	+6.3 Nov	+1.1	5.63	5.04	3.3	4.50	3.67
Hungary	-0.1 Nov	-11.3 Q3	-5.6	216	175	-3.4	9.47	9.00
Norway	+78.9 Dec	+86.5 Q3	+18.4	6.70	5.44	19.7	3.77	3.76
Poland	-24.0 Nov	-29.4 Nov	-5.6	3.30	2.45	-1.8	4.93	5.43
Russia	+189.4 Nov	+98.9 Q4	+6.0	33.9	24.5	5.5	13.00	10.85
Sweden	+17.2 Dec	+40.5 Q3	+7.3	7.97	6.37	2.4	1.13	3.02
Switzerland	+18.2 Nov	+40.3 Q3	+9.1	1.15	1.09	0.9	0.54	2.03
Turkey	-72.7 Nov	-43.9 Nov	-6.0	1.62	1.18	-1.5	14.31	7.79‡
Australia	-5.0 Nov	-56.7 Q3	-4.8	1.50	1.12	-0.3	3.45	4.06
Hong Kong	-26.0 Dec	+27.1 Q3	+10.0	7.76	7.80	-1.2	0.94	1.34
India	-112.3 Nov	-28.5 Q3	-4.2	48.9	39.4	-4.3	4.65	6.71
Indonesia	+12.1 Nov	+3.9 Q3	+0.4	11,310	9,288	-1.4	10.79	10.47‡
Malaysia	+42.2 Nov	+38.3 Q3	+12.8	3.59	3.24	-5.0	2.58	3.97‡
Pakistan	-21.8 Dec	-14.0 Q2	-5.7	78.9	62.6	-6.8	14.68	23.90‡
Singapore	+18.4 Dec	+29.2 Q3	+17.2	1.50	1.42	0.8	0.56	1.89
South Korea	-14.2 Dec	-7.9 Nov	-2.1	1,376	945	1.7	2.96	4.55
Taiwan	+3.9 Dec	+28.8 Q3	+6.4	33.6	32.2	-1.6	1.15	1.44
Thailand	-1.3 Nov	-0.6 Nov	-0.3	34.9	33.0	-1.4	2.22	2.85
Argentina	+13.2 Dec	+9.0 Q3	+2.7	3.49	3.16	0.2	16.69	na
Brazil	+24.7 Dec	-28.3 Dec	-1.8	2.29	1.78	-1.5	12.66	6.16‡
Chile	+10.2 Dec	-1.6 Q3	-2.5	612	466	4.5	7.20	3.91‡
Colombia	+2.0 Dec	-5.3 Q3	-2.4	2,352	1,935	-1.0	9.79	6.96‡
Mexico	-16.0 Dec	-11.8 Q3	-1.9	14.1	10.8	nil	7.31	7.60
Venezuela	+50.2 Q3	+49.4 Q3	+15.5	5.63	5.25§	-1.1	17.06	6.55‡
Egypt	-25.2 Q3	+0.1 Q3	+0.8	5.57	5.56	-6.8	11.37	4.64‡
Israel	-13.7 Dec	+2.6 Q3	+0.7	4.02	3.64	-1.2	1.23	3.37
Saudi Arabia	+150.8 2007	+95.0 2007	+30.3	3.75	3.75	10.7	1.22	na
South Africa	-10.6 Nov	-23.2 Q3	-7.8	9.89	7.30	0.2	10.95	7.91
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*								
Estonia	-3.9 Nov	-2.5 Nov	-10.6	11.8	10.6	-1.5	6.49	na
Finland	+10.2 Nov	+6.8 Nov	+3.5	0.76	0.68	4.6	2.09	4.04
Iceland	-0.3 Dec	-5.4 Q3	-17.3	115	64.8	0.3	18.27	na
Ireland	+40.7 Oct	-16.4 Q3	-4.9	0.76	0.68	-6.6	2.12	5.69
Latvia	-5.9 Nov	-4.8 Nov	-14.1	0.53	0.47	-2.7	9.01	na
Lithuania	-7.3 Nov	-6.4 Nov	-13.9	2.61	2.34	-0.9	8.37	na
Luxembourg	-7.5 Oct	+4.0 Q3	na	0.76	0.68	0.3	2.12	na
New Zealand	-3.8 Dec	-11.6 Q3	-9.0	1.87	1.28	-1.0	4.15	4.26
Peru	+4.0 Nov	-3.0 Q3	-2.8	3.16	2.94	2.7	6.50	na
Philippines	-7.5 Nov	+2.9 Sep	+2.6	46.9	40.8	-0.8	4.94	na
Portugal	-34.3 Oct	-29.3 Nov	-9.7	0.76	0.68	-2.4	2.12	4.59
Slovakia	-1.2 Nov	-6.7 Sep	-6.1	22.8	22.8	-2.3	1.35	4.23
Slovenia	-4.7 Nov	-3.4 Oct	-6.3	0.76	0.68	0.4	2.12	na

*Merchandise trade only. †*The Economist* poll or Economist Intelligence Unit forecast. ‡Dollar-denominated bonds. §Unofficial exchange rate.
Sources: National statistics offices and central banks; Thomson Datastream; Reuters; JPMorgan; Bank Leumi le-Israel; Centre for Monitoring Indian Economy; Danske Bank; Hong Kong Monetary Authority; Standard Bank Group; UBS; Westpac.



Markets

Jan 29th 2009
From The Economist print edition

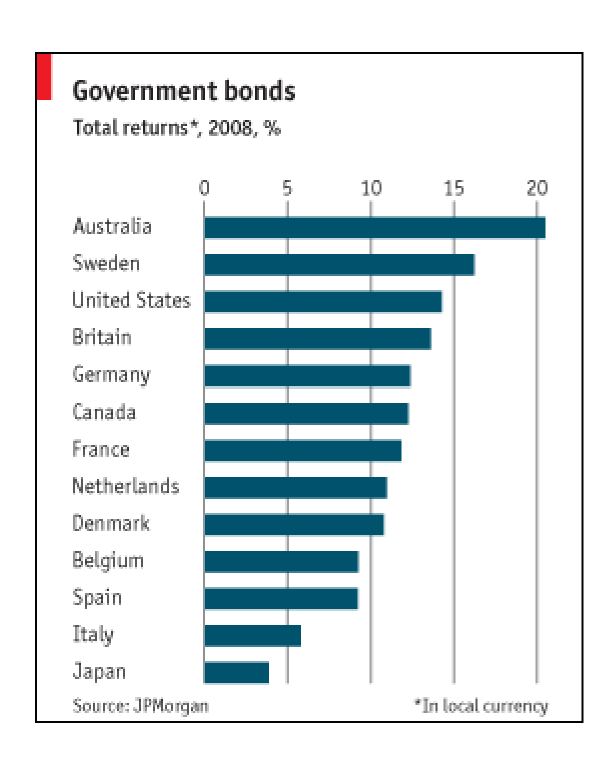
Markets

	Index Jan 28th	% change on one week	% change on Dec 31st 2007 in local currency	% change on Dec 31st 2007 in $ terms
United States (DJIA)	8,375.5	+1.8	-36.9	-36.9
United States (S&P 500)	874.1	+4.0	-40.5	-40.5
United States (NAScomp)	1,558.3	+3.4	-41.2	-41.2
Japan (Nikkei 225)	8,106.3	+2.6	-47.0	-32.5
Japan (Topix)	804.3	+2.2	-45.5	-30.5
China (SSEA)	2,089.9	+0.3	-62.1	-59.6
China (SSEB, $ terms)	124.8	+2.7	-68.1	-65.9
Britain (FTSE 100)	4,295.2	+5.8	-33.5	-54.1
Canada (S&P TSX)	8,906.2	+1.7	-35.6	-50.1
Euro area (FTSE Euro 100)	708.9	+6.0	-48.4	-54.6
Euro area (DJ STOXX 50)	2,322.8	+6.1	-47.2	-53.5
Austria (ATX)	1,713.5	+6.3	-62.0	-66.6
Belgium (Bel 20)	1,925.5	+7.3	-53.3	-58.9
France (CAC 40)	3,076.0	+5.9	-45.2	-51.7
Germany (DAX)*	4,518.7	+6.0	-44.0	-50.7
Greece (Athex Comp)	1,748.6	+2.7	-66.2	-70.3
Italy (S&P/MIB)	18,341.0	+3.7	-52.4	-58.1
Netherlands (AEX)	257.2	+8.2	-50.1	-56.1
Spain (Madrid SE)	923.7	+6.1	-43.7	-50.5
Czech Republic (PX)	786.4	+0.3	-56.7	-63.2
Denmark (OMXCB)	237.4	+2.3	-47.1	-53.4
Hungary (BUX)	11,925.4	+0.7	-54.5	-64.4
Norway (OSEAX)	282.7	+4.2	-50.4	-61.5
Poland (WIG)	25,039.6	-2.3	-55.0	-67.2
Russia (RTS, $ terms)	546.4	+3.1	-68.1	-76.1
Sweden (Aff.Gen)	192.3	+4.1	-43.5	-56.4
Switzerland (SMI)	5,417.9	+2.1	-36.1	-37.0
Turkey (ISE)	26,705.6	+8.0	-51.9	-66.1
Australia (All Ord.)	3,435.1	+1.2	-46.5	-59.5
Hong Kong (Hang Seng)	12,578.6	nil	-54.8	-54.6
India (BSE)	9,257.5	+5.4	-54.4	-63.4
Indonesia (JSX)	1,321.5	nil	-51.9	-59.6
Malaysia (KLSE)	879.6	+0.7	-39.1	-44.3
Pakistan (KSE)	5,139.9	+0.1	-63.5	-71.7
Singapore (STI)	1,766.1	+3.6	-49.0	-51.3
South Korea (KOSPI)	1,158.0	+4.9	-39.0	-58.4
Taiwan (TWI)	4,248.0	nil	-50.1	-51.8
Thailand (SET)	448.4	+4.0	-47.8	-49.6
Argentina (MERV)	1,105.5	+4.0	-48.6	-53.3
Brazil (BVSP)	40,227.0	+4.4	-37.0	-52.6
Chile (IGPA)	12,195.6	+3.5	-13.4	-31.0
Colombia (IGBC)	7,703.3	+3.1	-28.0	-35.3
Mexico (IPC)	20,145.2	+3.3	-31.8	-46.7
Venezuela (IBC)	35,147.5	-0.4	-7.3	-58.8
Egypt (Case 30)	3,867.6	+2.3	-63.1	-63.3
Israel (TA-100)	607.7	+4.3	-47.4	-48.4
Saudi Arabia (Tadawul)	4,796.9	+5.3	-56.5	-56.5
South Africa (JSE AS)	21,028.5	+4.9	-27.4	-51.3
Europe (FTSEurofirst 300)	810.8	+5.4	-46.2	-52.6
World, dev'd (MSCI)	878.8	+4.8	-44.7	-44.7
Emerging markets (MSCI)	533.1	+3.5	-57.2	-57.2
World, all (MSCI)	217.1	+4.7	-46.2	-46.2
World bonds (Citigroup)	785.1	nil	+7.5	+7.5
EMBI+ (JPMorgan)	395.3	+1.7	-8.8	-8.8
Hedge funds (HFRX)‡	1,032.0	+0.1	-22.4	-22.4
Volatility, US (VIX)	39.7	46.4	22.5	(levels)
CDSs, Eur (iTRAXX)†	152.3	-11.9	+201.0	+165.0
CDSs, N Am (CDX)†	208.4	-12.0	+167.5	+167.5
Carbon trading (EU ETS) €	11.8	+1.4	-48.4	-54.6

*Total return index. †Credit-default swap spreads, basis points.
Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; JPMorgan Chase; Bank Leumi le-Israel; CBOE; CMIE; Danske Bank; EEX; HKMA; Markit; Standard Bank Group; UBS; Westpac. ‡Jan 27th.

Government bonds

Jan 29th 2009
From The Economist print edition



The average stockmarket investor had a miserable year in 2008. By contrast, holders of government bonds did rather well, as falling interest rates lifted prices. Bonds that started the year with the highest yields had most scope for capital gains. That helps to explain why the return on Australian bonds was the highest in the 13 rich countries making up JPMorgan's global bond index. Short-term interest rates were also slashed in Britain and America, driving long-term rates down and bond prices up. Sovereign-bond investors in Japan, where interest rates were already low, did worst in local-currency terms. In dollar terms, however, Japan was the best performer in the index, thanks to the rising yen.